

**REPORT BY THE
AUDITOR GENERAL
OF CALIFORNIA**

**A STUDY OF THE STATE'S OFFICE SPACE
FACILITIES PLANNING GOALS,
POLICIES, AND RECOMMENDATIONS**



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August 16, 1990

C-972

Honorable Elihu M. Harris, Chairman
Members, Joint Legislative
Audit Committee
State Capitol, Room 2148
Sacramento, California 95814

Dear Mr. Chairman and Members:

The Office of the Auditor General presents a report prepared under contract by Institute for Law and Policy Planning concerning the State's office space facilities planning goals, policies, and recommendations.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Kurt Sjoberg".

KURT R. SJOBERG
Acting Auditor General

A Study of the State's Office Space Facilities Planning Goals, Policies, and Recommendations

**Submitted to the Office of the Auditor General,
State of California**

FINAL REPORT

August 10, 1990

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TABLE OF CONTENTS

Executive Summary	
Introduction.....	1
The Study.....	2
The Planning Process	2
Findings.....	3
Recommendations	4
 Chapter 1: Introduction	
Statement of Purpose.....	5
Capitol Area Plan	5
Sacramento Facilities Plan	6
Problem Statement.....	7
Approach and Methodology	8
Organization of the Report.....	9
 Chapter 2: Review of the Current Process and Planning Environment	
The State's Current Planning Process.....	12
The Planning Environment	13
Legal Authority of DGS for Implementing CAP.....	14
Other Factors	16
Capitol Area Development Authority (CADA)	16
Capitol Area Planning Committee.....	17
OPDM's Role in the Planning Process.....	17
The Funding Process.....	20
Procedural Review.....	21
Projections of Staffing and Space Needs	21
Comprehensive Database	22
Review of OPDM's Economic Forecasting Model	23
 Chapter 3: Reasons Why Capitol Area Plan Has Not Been Implemented	
Decrease in Anticipated Sources of Capital Outlay Funding.....	27
Limited Use of Alternative Sources of Funding.....	28
No Effective Structure.....	30
Capital Outlay Process Is very Cumbersome.....	32
No Pressure	33
No Leadership.....	34
Changed Conditions and Flawed Assumptions.....	34
 Chapter 4: Policy Analysis - Lease versus Own Issues	
Existing Policies	37
Alternative Means of Acquiring Office Space	37
Financial Implications of the Current Practices.....	39
Funding Choices.....	43
Levels of Lease-Supported Debt	43
Financing Techniques	44

Chapter 5: Policy Analysis - Consolidation and Location Issues	
Introduction and Definitions.....	51
Consolidation policies.....	52
Location Policies.....	53
Unexamined Implications of these Criteria	54
Benefits and Impacts of Consolidation and Location.....	54
Implementation of the Policies	55
Actual or Effective Policy on Consolidation.....	56
Impacts of Actual Policy	57
Changed / New Conditions and Assumptions.....	57
Consolidation Criteria	58
Recommendations	61
Chapter 6: Policy Analysis - Public Benefit Issues	
Transportation Impacts.....	63
Environmental Impacts.....	67
Child Care impacts.....	68
Energy efficiency impacts.....	68
Chapter 7: Policy Analysis - Older Office Buildings Restoration Issues	
State Policies on Older Office Buildings In Sacramento	72
Economic Feasibility of Restoration.....	73
Partial Funding of Special Building Repairs.....	75
Potential Additional Cost of Asbestos Abatement.....	76
Additional Restrictions for Historical Buildings	77
Recommendations	77
Chapter 8: Recommendations	
Planning Structure.....	82
Review of Plan Assumptions.....	82
Financing Methods	83
The Capital Outlay Funding Process	84
Planning Policies and Process.....	85
Appendices	
A: Summary of Survey on Other States' Facilities Planning Approaches.....	87
B: OPDM Planning Process	103
C. Capital Outlay Process Components and Time	106
D. Projections	111
E. Review of OPDM's Economic Forecasting Model	121
F. Comparison of Straight Lease vs. Lease Purchase Financing Models	127
G. Financing Techniques	150
H. Policies, Objectives and Actions from the Sacramento Facilities Plan.....	157
I. Definition of the Planning Areas.....	162
SELECTED REFERENCES	163
STATE AND CONSUMER SERVICES AGENCIES' RESPONSE TO THIS REPORT.....	167

Executive Summary

EXECUTIVE SUMMARY

INTRODUCTION

The Capitol Area Plan (1977) is a master planning document to guide the development of some 42 blocks surrounding the state capitol. The Sacramento Facilities Plan (1977) is the element of that plan providing the details for constructing state office buildings and parking structures in the area, and the metropolitan Sacramento area. Both plans recognized the likelihood of continuing rapid growth of demand for governmental services, and took a long-range overall view of the development.

In 1977 the state government was ending a period of growth in Sacramento during which no new office buildings had been constructed. Expanding agencies had moved into available leased space, with the result that their functions were scattered and their total rent burden was very high. The area just south of the capitol was deteriorating, the area to the north was stagnating, and traffic and air pollution were becoming matters of concern.

The Sacramento Facilities Plan made specific recommendations to counteract these undesirable conditions. These were:

- An office building program which would consolidate dispersed activities and reduce the proportion of leased space to ten percent or less within ten years. Agencies with statewide responsibilities would be located in the core area (within five blocks of the capitol). The plan addressed development of the area south of the capitol with low-rise buildings on quarter-block lots, with the goal of preserving the mixture of office and residential use.
- Constructing larger office buildings north of L Street to encourage economic growth in that part of the city.
- Reduction of traffic, parking congestion, and air pollution by locating near public transit and developing peripheral parking.
- Rehabilitation of older buildings to extend their useful lifetime and improve energy use.
- Financing new construction and rehabilitation by the most economical means available, with the emphasis on direct capital outlay.

Authority to implement the Sacramento Facilities Plan was given to the Department of General Services, which created the Office of Project Development and Management as the unit to oversee the program and carry out planning for agencies in need of space. The Office of Real Estate and Design Services, also within DGS, is concerned with the acquisition of property and with leasing of space.

By 1988 it had become clear that the goals of the Sacramento Facilities Plan were not being met. There was little new construction or significant rehabilitation. Leased space

had increased from 36 percent to 48 percent of the total with a sixfold increase in leasing costs. Transportation problems had worsened.

THE STUDY

Consultants were charged with determining the reasons that the Sacramento Facilities Plan has been so meagerly implemented and with providing independently developed information related to the state's policies and activities for planning and developing facilities and office space.

A policy study of a master plan asks whether the assumptions of the plan itself are valid, whether its recommendations are consistent and realizable, and whether a structure exists for carrying them out. This study examines the facilities acquisition process rather than concentrating on OPDM's procedures. No recommendations are made for specific facilities. Consultants found that information on the capital facilities acquisition process is not compiled in any one location. While much information was gathered through case studies, Consultants caution that the conclusions drawn from them will not necessarily apply in all situations.

A number of actors enter the process at different stages. Consultants were contracted to focus their attention on OPDM, but observe that the major decision-making is done outside of that office. While OPDM's procedures were examined, it proved impossible to explain the failure to implement the Sacramento Facilities Plan without expanding the scope of the study to the overall planning system.

THE PLANNING PROCESS

Planning at the level of the Sacramento Facilities Plan may be visualized as consisting of three stages. The first stage consists of plan preparation; a master plan is prepared giving a comprehensive long-term view of the entire area under consideration. This process is essentially technical in nature, but decisions on location and size are always based on a combination of objective criteria and the planners' professional judgment.

The second stage requires making the decision to implement the master plan. As it involves the allocation of resources among competing agencies it is unavoidably political. New priorities are communicated to the planning office, and a revised master plan is submitted.

Finally, the plan as accepted is implemented; individual facility plans are drawn up and the buildings are constructed. Once again this is a technical activity.

Although in the second stage, decisions are made about priorities and what actually gets built, all stages involve making certain types of decisions. In the master plan these are made broadly, considering the interaction of all parts of the plan. At the implementation stage many of the same types of decisions are made in much greater detail and specificity. These decisions are, in summary, whether to consolidate or disperse agencies, where to locate them, how large to make them (for now and for the future), and how to pay for it all. Guiding all these decisions are the needs to save money and to make the most beneficial impact on both the building occupants and the environment.

FINDINGS

Consultants have reviewed OPDM's overall planning procedures, and the description of the findings is given at length in the body of this report. Although a number of specific recommendations for improving planning processes and procedures are made, in general, Consultants found that OPDM's procedures are well-suited to perform the task with which they have been charged. Although individual practices may contribute in minor ways to lack of implementation, the major reasons for the lack of implementation are beyond the scope of OPDM.

The reason which is most widely cited for the failure to build is that sources of direct capital outlay have dried up. This is indeed so; it is, in general, now impossible to construct a building from funds on hand. However, alternative funding methods are, and always have been, available to those who would use them.

The real reason that there has been no new building is that this has not been a priority for state decision makers. In a few recent instances, mostly outside of Sacramento, when buildings have been a priority they have been built.

The result of the current policy is that the state is spending, and will continue to spend, a great deal more money than it needs to in providing facilities. In the long run, leasing facilities is far more expensive than owning them. (Paradoxically, it is cheaper to lease for the first few years, so that when space is needed only temporarily, leasing is the appropriate path.) To say that there is no money to build ignores the fact that the state has the money and is spending it now on leases. Costs of leasing continue to grow, unless positive steps are taken to institute a building program.

Specific findings include the following:

- There has not been effective leadership at a high level to ensure that the Sacramento Facilities Plan is implemented.

- OPDM has limited resources to maintain the plan and virtually no authority to implement it. Control over the capital acquisition process is dispersed and ill-defined.
- The procedures for obtaining authority and funding to build are complex, uncertain, and extremely time-consuming. Faced with these, many agency heads opt to lease.
- Capital outlay funds have essentially disappeared.
- The state has, nevertheless, made very little use of alternative financing schemes.
- The ready availability of leasable space, at reasonable rents, has reduced the demand for construction by relieving overcrowding pressures.
- Some assumptions of the original Capitol Area Plan are flawed, and some of the conditions under which it was developed have changed. Building north of L Street and building on quarter-block lots turn out to be impractical in most cases. Reducing leased space is highly desirable, but there is no basis for using the arbitrary and inflexible goal of ten percent leased space overall.

RECOMMENDATIONS

Consultants believe the Sacramento Facilities Plan is fundamentally sound and that, with a few specific exceptions discussed below, implementation of the policies set forth in the plan will provide maximum public benefit to the citizens of the state. Consultants have made, in the body of the report, a number of recommendations for improving implementation of the Sacramento Facilities Plan. However, none of the specific problems that these recommendations address will automatically result in plan implementation. The state must address the underlying reasons for the failure.

Consultants stress that the basic recommendation addresses the lack of leadership.

The state of California, including the new administration and the legislature, must decide if it still wishes to implement the Capitol Area Plan and the Sacramento Facilities Plan. If it does (or has only minor modifications), a clear commitment to do so is required.

Chapter 1

Introduction

CHAPTER 1 INTRODUCTION

STATEMENT OF PURPOSE

The Institute for Law and Policy Planning (hereafter referred to as Consultant) conducted a study of the state of California's office space under contract with the Office of the Auditor General. The purpose of this study is to provide the legislature with independently developed information related to the state's policies and activities for planning and developing facilities and office space as presented in Sacramento Facilities Plan, Eighth Supplement: Implementation Issues, 1988.

The issues discussed in the Eighth Supplement raise three key questions which form the core of this study.

1. What is the most effective method of coordinating and consolidating the state's office space needs?
2. What are the cost implications of the current policy?
3. What are the public benefits arriving from the implementation of the current policy?

In 1977, the legislature adopted a Capitol Area Plan (CAP) to coordinate the development and use of state facilities in metropolitan Sacramento. The OPDM, in response to the 1977 CAP, published the Sacramento Facilities Plan, 1977-2000. This document laid out policies, plans and recommendations to fulfill the legislature's goals as expressed in the CAP.

Acquisition of office space for the state of California, whether through purchase or lease, is primarily the responsibility of the Department of General Services (DGS). The Office of Project Development and Management (OPDM) manages the state's capital outlay construction program and plans the development of state offices and parking facilities. OPDM is also the official "caretaker" of the Capitol Area Plan.

CAPITOL AREA PLAN

The CAP focused on the state's presence in, and impact on, the core area of the city. Assumptions and guidelines were incorporated, and key policies reflected concerns for conservation, mixed use, and pleasant human environments.

Though it recommends specific actions to interpret the policies, the essential purpose of the CAP is to serve as a guide for an ongoing state planning and development

process in downtown Sacramento. Long-term goals and objectives, and policies to achieve these, were specified for each element of the plan. The ten elements of the plan are:

- state office space
- Transportation
- Parking
- Housing
- Community development
- Open space
- Public amenities
- Energy use
- Relations of the state to local government
- Plan administration.

One of the policies of the state office elements is to "meet projected needs for state office space in the core area in a cost-efficient manner, including new construction of state-owned offices and rehabilitation of existing structures to office use." The plan proposed setting up an administrative structure to perform the development and coordination function as well as a mechanism for assuming community input. These were accomplished by setting the Capitol Area Development Authority (CADA), a joint power authority between the state and city, to act as developer. The Department of General Services was designated coordinator, and a Capitol Area Planning Committee (CAPC) was set up to provide community input to the development process.

The financial implications of the plan were discussed and four capital financing alternatives were recommended for use as appropriate.

SACRAMENTO FACILITIES PLAN

The Sacramento Facilities Plan 1977-2000 is an element of the Capitol Area Plan, and was prepared by the Department of General Services (DGS) Long Range Planning Unit (which later became OPDM). The document laid out DGS' policies, plans, and recommendations to fulfill the legislature's goals. The primary purposes of the plan were to 1) identify the relationships between state governmental entities; 2) project office space needs; and 3) propose policies and actions which would result in sound economic, social, and environmental development and use of office facilities. See Appendix H for a summary of policies and actions from the Sacramento Facilities Plan.

Since the original facility plan was published in 1977, eight supplements have been published evaluating the progress toward implementation of the goals and impact of the policies. In 1988, OPDM issued the Sacramento Facilities Plan - Eighth Supplement: Implementation Issues. This 8th Supplement, in addition to updating the information provided in previous supplements, set forth questions related to goals and policies of the previously adopted Capitol Area and Sacramento Facilities Plans.

PROBLEM STATEMENT

The Sacramento Facilities Plan made specific recommendations. Principal among these were:

1. An aggressive office building program which would allow consolidation of dispersed activities and reduce the proportion of leased space to 10% or less within 10 years. The offices of agencies with statewide responsibilities would be located in the core area (within 5 blocks of the capitol).
2. Development of the area south of the capitol with low-rise buildings on the scale of quarter-block lots in order to preserve the mixture of office and residential use.
3. Constructing larger office buildings north of the capitol, that is, north of L Street, to encourage the economic growth of that part of the city.
4. Reduction of traffic, parking congestion, and air pollution by placing buildings near public transit, developing peripheral parking, and otherwise reducing the fraction of single-occupant vehicles.
5. Rehabilitation of older buildings to extend their useful lifetime and improve their use of energy.
6. Financing new construction and rehabilitation by the most economical means available, with the emphasis on direct capital outlay.

By 1988 it had become clear that the goals of the Facilities Plan were not being met. Four office buildings were put up in the late 1970s - three of them in the core area - and then the program stalled despite a rapid increase in state government employment. There was no more new construction and no significant rehabilitation except to mitigate fire and life safety concerns.

Private development of office structures in the area north of L Street had blossomed, and the state had become a major tenant in many of these buildings. The proportion of leased space had increased, not decreased, and sub-units of agencies continued to be scattered. In 1977, state-owned space represented 64 percent of state office space in Sacramento. By 1989, the proportion of state-owned space had fallen to 52 percent. In fact, between 1977 and 1989 total leased space more than doubled and annual leasing costs increased more than sixfold - from \$10.1 million to \$65.5 million. Transportation problems worsened. The fraction of single-occupant vehicles grew and parking became more difficult. The dispersal of offices increased the need for driving and decreased energy efficiency.

These major failures at the heart of the plan were explored in the Eighth Supplement to the Sacramento Facilities Plan (1988).

APPROACH AND METHODOLOGY

This study provides analysis, evaluation, and recommendations on the procedures and available resources of OPDM and the policies under which they operate. The findings are based on examination of documents, data, schedules, literature review, and interviews. Because of the complexities of policy issues, specific written procedures were often not available, and Consultants relied on information gained from interviews.

The primary source of data for this study is the Department of General Services because of its responsibility in coordinating the state office space program. OPDM and the Office of Real Estate and Design Services (OREDS) are offices within DGS that produced much of the primary data used in this study. Other sources are the Office of the State Architect (OSA), the Telecommunications Office, and Building and Maintenance.

Secondary sources include the city of Sacramento, CADA, Department of Finance, the Legislative Analyst's Office, and other departments selected as candidates for case studies to illustrate OPDM's office facilities planning process. Information was also obtained from a survey of selected states regarding facilities planning approaches that California can emulate.

The methodology used in this study combines a number of approaches due to the complex nature of the issues involved. The methods used include content analysis, quantitative techniques, case studies, survey research and process evaluation.

Content analysis and process evaluation were primarily used to address the issue of coordination and consolidation of space needs. The approach first specified the current methods and procedures for locating buildings and for deciding whether or not to consolidate in specific areas of Sacramento. Second, the approach assessed the actual practice to determine if these processes and procedures were followed. Third, it compared methods and procedures with accepted professional practice. Fourth, case studies were used to exemplify the methods and approach used in the planning for state office space.

A quantitative analytical technique was used when determining the causes and financial implications of the current capital outlay process. The comparison of the straight lease and lease-purchase financial alternatives was done quantitatively. Assumptions as to the behavior of financial factors were specified and a comparison of the two methods was performed using three time horizons - five years, break-even point and 50 years. OPDM's Economic Forecasting Model (EFM) was assessed for completeness of variable specifications and internal consistency of assumptions. The identification of financing

techniques, and the reasons why the state has leased more office space than anticipated were process evaluations.

Case studies were used extensively. For example, case studies were used to determine the economic feasibility of rehabilitation, and the availability of funding for renovation. Survey research methods were also used to find out how other states go about restoring older buildings. A telephone survey was conducted and responses from twelve states were tabulated for analysis.

Face to face interviews were conducted to solicit opinions from informed persons relative to the facilities planning process of the state. Consultants also conducted a survey of other states to compare their facilities planning methods with California's. The results of this survey can be found in Appendix A.

ORGANIZATION OF THE REPORT

This report contains eight major chapters. First is this introduction, followed by a review of the current process and planning environment. Chapter 3 discusses the seven reasons that contribute to the lack of implementation of the CAP. Policy analysis is then presented in the next four chapters. The first of these, Chapter 4, addresses the question of lease versus own. Chapter 5 addresses consolidation and location issues. Chapter 6 discusses public benefits. Chapter 7 studies the restoration of older state-owned buildings. Although some of these chapters contain recommendations that flow logically from the discussion of analysis and findings, all recommendations are summarized (with brief explanations) in Chapter 8, Recommendations.

Consultants' reference materials follow. The report ends with Appendices A through H which present technical data and discussions relevant to the study. These appendices are referred to throughout the body of the report.

Chapter 2

Review of the Current Process and Planning Environment

CHAPTER 2

REVIEW OF THE CURRENT PROCESS AND PLANNING ENVIRONMENT

This section contains both a general review of the planning environment, including OPDM's legal authority and the roles of other actors, and a specific review of several planning procedures used by OPDM. These planning procedures include locational decision making, the economic forecasting model, projections methodology, and the planning data base. The purpose of reviewing the facilities planning process is to determine the extent to which current planning practices contribute to the failure to implement the Sacramento Facilities Plan.

This is a policy study: it reviews the policies and approach of the state's planning efforts. It does not seek to answer specific planning questions, nor is it primarily a technical review of planning procedures. Individual plans were examined not for specific findings but rather to determine process, criteria, and comprehensiveness.

Consultants find that, on the whole, OPDM's planning procedures are based on sound professional practice and criteria. The major shortcoming pointed out in the following discussion is that when projects are analyzed only one project at a time, implementation of an overall plan is not emphasized. Although this contributes in a minor way to lack of implementation, the major reasons for the lack of CAP implementation are explored in Chapter Three.

Because of the scope and short time frame of the study, analysis was limited by a scarcity of readily available data. Much useful information is not preserved in easily accessible form, in particular the history of successful and unsuccessful projects which would yield valuable insights into the actual, as opposed to the nominal, workings of the process. In consequence certain features of the space acquisition process remain unclear. This lack of data appears to have two causes. The first is the number of agencies involved, and the lack of mandate to any one agency to be responsible for accumulating all agencies information. The second reason is the relatively late computerization of the planning process and data.

OPDM does not have a full set of standard procedures that it uses in the planning process. Consultants, recognizing the complexity and uniqueness of each facility plan, do not necessarily believe that it is possible or even desirable to have such procedures.

Consultants have two specific recommendations regarding this issue. First, a more comprehensive description of the Capital Outlay Budget Process would assist everyone involved in the process.¹ While there are several documents (prepared by either the Department of Finance or OPDM) that currently describe the process, Consultants believe the explanation could be substantially improved and diagrammed. The report should include legal and historical parameters, a determination of capital budget funding limits, the annual capital budget and five year improvement program (including time frames for funding cycles), and a description of capital budget implementation. Inclusion of other related information on the planning process, such as the leasing process, might also be helpful.

Second, Consultants strongly support the idea of a comprehensive multi-year capital outlay program for the state. Consultants tried to follow the progress of individual buildings through the planning and construction steps to determine where problems exist, and why the plan is not being implemented. However, the information needed for such case studies does not exist in one place. To obtain this information, Consultants would have to review the Five-year Capital Outlay Program from both DGS and individual agencies, Governor's Budgets, and Legislative Analysts Reports that cover a range of at least ten years. In addition, the working drawing, estimating, bid, and construction information for each project would have to be reviewed. A comprehensive capital outlay program would provide much of this information in one place.²

THE STATE'S CURRENT PLANNING PROCESS

The planning process for capital facilities can be thought of as comprising three stages. First is the plan itself: a description of buildings proposed for construction or restoration, their locations, sizes, and effects on their surroundings. Devising a financing scheme for the construction is an essential component of the plan. Planning in this sense is primarily a technical activity. On a large scale planning level, this activity is primarily carried out by OPDM, although individual agencies have considerable input.

Second is the decision-making process: deciding what parts of the plan are to be implemented and obtaining the funds to do so. This activity is highly political. It is unlikely that all parties affected by a plan, especially a comprehensive area plan, will be

¹See Appendix B - Capital Outlay Budget Process. See also "Capital Outlay Budget Process," DOF, 6/21/90.

²Consultants conducted a survey of facility planning in other states. The State of Maryland has several documents that present similar concepts. See Appendix A.

equally delighted with the changes proposed for them. A workable compromise must be arrived at, and this must include the cooperation of the funding authorities.

It is apparent that OPDM does not have responsibility for the intermediate, and crucial, stage of decision-making (which includes setting planning priorities). Consultants believe this responsibility does not devolve upon any well-defined or accountable actor, but is diffused and is strongly influenced by informal and ad hoc political considerations. To a large extent decisions are not made here at all, but rather in the implementation phase where they are attacked piecemeal.

Finally there is plan implementation. If the decision-making stage has been properly carried out this is again reduced to a technical activity: detailed specifications, contracting out and supervising the construction, scheduling moves, etc. Because of the inevitable unexpected complications which will arise, this stage must continue to be coordinated with the decision-making actors, but that should not be the primary activity at this point. Responsibility for this phase is largely OPDM's, but the Department of Finance (DOF), client agencies, and OSA are strongly involved.

The process consists of a technical stage, a political stage, and another technical stage; clearly the second step will be carried out by a different entity from the other two. Decision-makers need not have technical skills; they need the authority and leadership to make and enforce the decisions, which planners do not usually have.

THE PLANNING ENVIRONMENT

The issues that must be considered in a review of the Capitol Area Plan and the Sacramento Facilities Plan are extraordinarily complex, and they occur in a complex planning environment. A thorough analysis of why the policies of these plans have not been implemented must include not only an understanding of specific policies and procedures, but also an understanding of the overall context. This includes the state's planning and decision-making process, how different agencies (often with competing views) interact, and an understanding of the capital outlay process. The analysis must also acknowledge that these decisions are not simply the results of any individual agency's actions, but are part of a political process that involves the legislative and administrative powers of the state.

LEGAL AUTHORITY OF DGS FOR IMPLEMENTING CAP

The Department of General Services (DGS) was formed in 1965 by the legislature because of the need for centralization of business management functions and services of state government. To meet the legislative mandate, DGS was given broad authority, which included planning, acquisition, construction, maintenance and police protection of state buildings and property, purchasing, architectural services and accounting services. (See Government Code §14660.)

Because DGS was created by statute, all of its power and responsibilities are defined by statute. (See Government Code §14600 et seq.) The director of DGS has been given the authority to establish OPDM with specific powers derived from Government Code §8160 et seq. and general powers. As a result, OPDM's authority is dependent upon two factors: the scope of authority given to DGS by statute and the responsibilities delegated by the director of DGS in the exercise of that statutory authority.

All contracts for the acquisition or hiring of real property by state agencies must be approved by DGS. (Government Code §11005.) Even if the Department of Finance has approved an agency's budget for a specific project, the state agency must also obtain DGS approval of the contract, lease transaction or expenditure. (See Government Code §13325.)

The Capitol Area Plan included a recommended administrative structure which was instituted when the legislature adopted the Capitol Area Plan in 1977.

First, the plan recommended establishment of a joint powers authority to function as the "master developer" for the capitol area housing component and those projects delegated through DGS Development Ground Leases. This recommendation was enacted as Government Code section 8169.4 and led to the establishment of CADA. Second was the recommendation to establish a Capitol Area Planning Committee to advise DGS (Government Code §8164.1). The third and final component of the recommended structure was a "Capitol Area Plan Office" within DGS to administer, update and coordinate implementation of the plan. There is no specific statute to create such an office. Instead, the legislature specifically gave the Director of DGS responsibility and authority for the formulation and implementation of the Capitol Area Plan. (See Government Code §8166, §8168-§8169.3.)

OPDM's responsibilities and authority are set forth in the State Administrative Manual, §1300 through §1305. Although a predecessor to OPDM was originally created to

"administer, update and coordinate" implementation of the Capitol Area Plan, that goal is now secondary to OPDM's "primary responsibility" to determine future space requirements for all state agencies, develop area facilities plans and formulate recommendations for meeting space requirements. (Moreover, OPDM's responsibilities are not limited to the capitol area; they have been expanded to include both major and minor metropolitan areas throughout the state.)

OPDM's specific responsibilities with respect to the Capitol Area Plan have been reduced from those originally outlined in 1977. OPDM now is responsible only for "maintaining and updating the Capitol Area Plan." (See State Administrative Manual, §1305.) It no longer has express authority to administer or coordinate implementation of the Plan. OPDM has been given authority only to review capital outlay projects involving office construction, which represents but one "element in the immediate environment." OPDM also has authority to review and approve all space requests, but the actual programming, planning and leasing are performed by another interdepartmental entity, the Office of Real Estate and Design Services (OREDS).

The Capitol Area Plan was intended to be a "guide for future state policy" in the expansion of the state's physical plant and in the location of state buildings and other facilities in the Sacramento metropolitan area. (See Government Code §8163, §8166.) The statutes, however, make implementation of short-term options more feasible than those consistent with long-range goals. Government Code §14669 authorizes DGS to lease property for the use of any state agency. Although such leases are generally limited to a five-year term, the director can enter into a longer lease agreement by giving thirty days notice to the chairpersons of designated legislative committees. No other legislative review is required. (See Government Code §13332.10.) In contrast, the director may not enter into a lease-purchase or lease with an option to purchase (initial option purchase price over two million dollars) without specific authorization from the legislature.

This legislation may easily lead to the implicit assumption that one entity (OPDM) is charged with determining the location of all state offices. This would require a pro-active and systematic approach. The reality, as this study finds, is that there is no such entity. OPDM and OREDS have not been mandated to pro-actively plan for the office space needs of all state agencies. While the parameters of DGS authority have been set by statute, there are legal and environmental constraints on the exercise of such authority.

OTHER FACTORS

In addition to the policies set forth in these plans, there are a number of factors that add complexity to the planning process. These include the California Environmental Quality Act (CEQA) which applies to any facility constructed. The historic character of buildings over 50 years old cannot be lightly regarded in restoration. All new facilities must lie within a quarter mile of a "transportation corridor" (all space in the core area complies), and the state has set itself the goal of reducing single-occupancy vehicles to not more than five percent of total state employees.

Energy conserving features must be included in new buildings and retrofitted into older ones where practical. All facilities must be made accessible for the handicapped, and space for child care programs must be set aside in all large new or substantially rehabilitated buildings. (The child care programs themselves are not mandated.)

CAPITOL AREA DEVELOPMENT AUTHORITY (CADA)

The Capitol Area Development Authority (CADA) is a joint powers agency to implement the goals and objectives of the Capitol Area Plan which was adopted by the legislature in 1977. Governed by a five-member autonomous board, CADA coordinates policy and planning input. Two board members are appointed by the state's Department of General Services, two are appointed by the city of Sacramento, and these four appoint the fifth member.

Although a relatively small development authority, CADA has developed over 300 new housing units in the capitol area, and completed rehabilitation of over 300 commercial units. It is currently working on the development of its first office building.

Because CADA can issue bonds, and could perhaps expedite the currently time-consuming and cumbersome process of office building development, there has been some discussion of its role as a means of office space development in the core area. CADA has not, however, had the political leadership from the various political representatives on its board and advisory committees to proceed with such development. Instead, CADA has concentrated on housing, commercial rehabilitation, and the important property maintenance functions involved in managing the state's land interests in the core area.

CAPITOL AREA PLANNING COMMITTEE

In the legislation adopting the Capitol Area Plan, there is a provision for a Capitol Area Planning Committee, consisting of nine members, who serve four-year terms. Four of these members are appointed by the governor (at least one from a list of three candidates submitted by the city of Sacramento and at least one from a list of three submitted by the county of Sacramento). Two members of the Committee are appointed by the Speaker of the Assembly. Two members are appointed by the Senate Rules Committee, and one member is appointed by the Director of DGS. These positions are not paid, but members are reimbursed for expenses. The committee also has an advisory board that serves without compensation.

OPDM'S ROLE IN THE PLANNING PROCESS

OPDM is authorized to perform two related planning tasks. First, it is responsible for the maintenance of the Capitol Area and Sacramento Facilities Plans as well as regional planning. OPDM's second, and more frequent, task is to plan for the construction or restoration of individual facilities. The agencies involved at the implementation stage initiate the process and contract OPDM to do the planning. Although it is appropriate that a single agency be responsible for both planning and implementation so that facility studies will automatically be set in the context of the master plan, there is an inherent contradiction in these two types of activity. Concentrating on individual facilities runs the risk of optimizing the solutions for those facilities alone with possible adverse consequences for the plan as a whole.

Maintenance of the plans is a master planning function which involves looking at the state of office facilities as a whole: inventorying and assessing the condition of all buildings, forecasting the demand for space over the next ten years or so, deciding who could be located where, whether new buildings should be built or old ones rehabilitated (or abandoned), what the large-scale environmental and transportation impact would be, and how best to finance the whole program. This is the first stage of the overall planning process earlier described.

OPDM's efforts in the overall plans seem to be confined to updating the planning information and preparing the annual progress reports. This task should not be underestimated; reports have contained many salient observations and suggestions as to modifications needed in light of external changes.

While OPDM provides planning services to other agencies, its ability to move an agency which does not want to be moved, to prevent an agency from choosing to expand through leasing, or to stipulate the exact location for those who do wish to move, is extremely limited. If there is disagreement, OPDM seems to be limited to comments and advice to the DOF and the legislature. (Such disagreements can revolve around the issues addressed in environmental impact reports.)

In addition, some directives of the plan are carried out by other offices or departments. For example, the General Services Buildings and Grounds division is responsible for much of the rehabilitation and repair component of the Sacramento Facilities Plan. The Office of the State Architect is also involved in analyzing and projecting technical requests such as asbestos abatement programs.

The second major area of OPDM's responsibility for planning is assisting with individual facility plans. This is a complex and lengthy process involving a number of actors. OPDM is able to enter into a great deal more detail than in the master plan and take into account the special needs of each particular client. In this task, OPDM tends to defer to the wishes of the client agencies. It normally accepts the client's choice of location and facility size. A more complete discussion of OPDM's planning process for individual facilities is included as Appendix B.

Each agency identifies its own needs and then requests either OPDM or OREDS to respond. If the request is for leased space, the agency submits a Form 9: Space Action Request Form to OREDS. OPDM reviews the forms for information regarding the Sacramento Facilities Plan, to assist in scheduling anticipated environmental workload. OPDM does not initiate the space actions indicated by the master plans.

The determination of where a given department should be located depends on whether the requesting agency wants to build or lease, and when the space is needed. If the requesting agency wants to construct a state-owned building, OPDM works with the agency to plan the location. If the requesting agency wants to lease, then OREDS is responsible. The Department of General Services does not make an independent decision on which agencies should move or where they should go.

When providing these services, OPDM enters into a consultant-client relationship with the agency. OPDM makes a rather detailed study of the client's needs. (This level of detail must be considerably more complex than that used when updating the plan as a whole.) Existing space is described, including size, layout, location, building condition,

special space needs, building tenure, transportation, parking, visitors, and program. Detailed staffing and space projections are made.

On the basis of the existing conditions and the anticipated needs, OPDM next considers the alternative courses of action. The four basic options are for the agency to remain in its present space, to move to other state-owned space, to lease new space, or to acquire a new facility. There is seldom any unused space currently available in state-owned buildings, but OPDM can use the findings to help justify the needs for a new multi-tenant facility.

The choice among the four options is made on the basis of a number of criteria. These are: building size and cost, financing options, program needs, location needs, existing plans, need to consolidate or split, access, parking, and transportation issues, environmental concerns, external political and economic factors, and scheduling and timing. All of these can be specified, but only the first two can be quantified. Worse, there is no objective way to evaluate the relative importance of the different criteria, nor to assign weighting to the ordinal values ("good," "fair," "poor") which most of them assume.

This demonstrates the problem inherent in any planning process: how to make a choice on the basis of criteria among which there is no precise numerical relationship. (Cost alone is inadequate since the cheapest option always is to do nothing.) There is no standard way to make this decision, as the process is not the same in every case. The decision rests on the judgment of the planner, and the client agency must agree. It appears to Consultants that outside political pressure is one of the more important factors in determining the final choice.

Consultants find that OPDM carries out the process as described in a responsible and competent fashion. However the process itself is linear and specific to the project under consideration. It does not incorporate feedback loops where the findings at intermediate stages are examined to see whether they satisfy, or modify, the original problem. In particular, the results should be related back to the goals of the Capitol Area Plan, such as reducing leased space, improving transportation, and consolidating functions. Dividing the leasing and acquisition functions between two separate units of DGS raises a major barrier to the holistic approach envisioned in the plan.

OPDM is the principal project manager for state office building construction. Design-related services, including assessment of older buildings, may be provided by OSA or by private architectural and engineering firms. OREDS devises plans for leasing space in much the same way that OPDM does for property acquisition. Finally, the Office of

Buildings and Grounds is responsible for building maintenance; in its larger projects it overlaps this rehabilitation function. (Assistance in providing state office space is only a portion of the workload of these offices; other functions are not discussed in this report.)

The Department of Finance, the governor, the Legislative Analyst, and the legislature are all involved in scrutinizing requests for project funding; their roles will be discussed in conjunction with the capital outlay process itself. If a facility is to be financed by the issuance of bonds by the state, the state Treasurer will have a voice in that as well.

THE FUNDING PROCESS

The state has traditionally funded new or restored facilities through direct capital outlay. (A complete description of the Capital Outlay Budget Process is presented in Appendix C.) Obtaining funds in this way is a lengthy process with a number of pitfalls along the way. The process itself is an impediment to capital facilities acquisition.

Each department or agency prepares a five-year capital outlay plan. This is not in itself a request for funding, only a statement of intent. When the agency actually wishes to acquire new space, it may develop a facilities plan on its own (not all agencies do this very well) or contract with OPDM for a plan. DGS itself, through OPDM, is one of the most likely candidates for this since it will, in general, be the owner of any new general-purpose, multi-tenant office buildings.

The completed plan is submitted for inclusion into the state budget as a Budget Change Proposal (BCP) for preliminary architectural plans. The first agency to review the proposal is the Capital Outlay Unit of the Department of Finance. Next it goes to the governor for approval; if it is included in the governor's budget it is next examined by the legislative analyst. Finally it goes to the legislature (through appropriate committees). At any one of these stages, the project can be deleted.

If the preliminary plans are approved, a request is submitted for working construction drawings. Because of the deadlines of the budget cycle it is often necessary to apply for the drawings before the preliminary plans are completed, which complicates the description of those drawings since it is not entirely clear what they are based on. If the plans are funded, the process is followed still once again with a request for construction funds. The same mismatch with the timing of the budget cycle occurs.

At various times in the past, plans and even drawings were funded only to have the construction stage disapproved. The architectural expenses were wasted (and these were about 5 percent of construction costs, not an insignificant sum). Even if the building had

been revived several years later the plans might have become outdated. The Department of Finance has now changed its practices so that the most careful scrutiny is given at the time of the request for plans; if this passes, and includes a credible financing plan, the drawing and construction phases will be approved unless there is an inordinate escalation of the costs.

This process, when all goes perfectly, takes at least five years from the time of the first facilities plan to occupancy of the building. Matters do not usually proceed that smoothly. For example, the original facility plan for the Ronald Reagan Building in Los Angeles was prepared in 1975, and the architectural plans were funded in 1980. The building is scheduled to be occupied in late 1990. Consultants estimate that a private developer could complete in two to four years the process which takes the state seven to nine years.

Compare this with the time to lease office space: although legislative approval is required, an agency can normally move in within 6 to 18 months after the request, and the staff time and effort to win approval is far less. It is not at all surprising that, confronted with the option of leased space in about a year versus a highly uncertain building process consuming most of a decade, agency heads will choose the simpler and surer path, especially since rents in Sacramento are not exorbitant (compared with those in San Francisco or Los Angeles).

PROCEDURAL REVIEW

Three aspects of OPDM's procedures have been reviewed. These do not constitute the entire planning process but they are essential to it. These are primarily technical matters with no important policy issues connected to them (other than the question of "Who does it?").

The first of these procedures reviewed involves the projection of future needs, the second concerns the maintenance of the database on which the analysis is based, and the third is the means by which the best method of financing is found for each proposed project. More complete and detailed discussions of these can be found in the appendix.

PROJECTIONS OF STAFFING AND SPACE NEEDS

Maintenance of the Sacramento Facilities Plan requires a periodic update of the anticipated space needs for the entire Sacramento work force. Consultants conducted a technical review of this projection methodology. A full discussion of the review and

findings are presented in Appendix D. The following discussion summarizes the discussion and findings.

The procedure for projecting staffing at the plan level is based on the staffing expectations of agency heads. These staffing projections are compiled, generally without criticism, and translated into rough space figures by allotting 150 square feet per new employee. Generally, Consultants find this to be an acceptable practice for predicting overall space needs, especially in view of the very limited resources allocated to OPDM for carrying out this task. The 10-year total staffing projection made in 1978 agrees quite well with the actual total staffing in 1988. This seems to be due to the cancellation of opposing errors, however, since the forecasts for a number of individual departments were spectacularly in error.

Consultants recommend that the staffing forecasts be supplemented with techniques which do not depend so heavily upon the agency's own assessment. Examination of historical staffing patterns will help remove the subjective element in these predictions.

Consultants independently projected the total Sacramento staffing as a function of total state population. On the assumption that Sacramento employment as a function of population will continue to decrease slightly for a few years, especially in view of the current funding crisis, and will then stabilize, Consultants project a Sacramento area office population of 52,500 in 1993 and 55,000 in 1998. These are about 5 percent lower than OPDM's projections for the same dates. Consultants' figures, if extended to 2003, would approximate what OPDM predicts for 1998. Consultants have not made projections for individual departments.

Staffing is driven primarily by state population, but is subject to influence by all manner of external circumstances: the national and local economy, shifting program priorities, public inclination toward government in general, and special issues affecting economic or social conditions. It can never be predicted infallibly; the only safe course is to prepare a range of projections under different sets of assumptions and continually update them to reflect the most recent data.

COMPREHENSIVE DATABASE

Fundamental to the task of planning, and to the whole task of facilities management, is the maintenance of a comprehensive and accurate database. Consultants applaud the establishment of the Statewide Property Inventory (SPI) under OREDS to serve as this basic tool. To avoid inconsistencies, Consultants recommend that only this

database be used for facilities planning, supplemented where necessary, by other information not contained in it. OPDM should have immediate read-only access to the SPI and should transmit updated or corrected information to OREDS for input.

Any property which is excluded from the SPI will lessen its usefulness. Therefore, an effort should be made to obtain information even on those facilities which have been exempted, specifically the information pertaining to the staffing and property of the legislature since it is an important, if uncounted, component of the Capitol Area Plan.

Consultants have examined the field structure of the SPI and find that it appears to contain the information needed for comprehensive planning, with one exception: the suitability of the property for use in asset substitution (the recommended short-term financing technique). It may be possible to insert this quantity into one of the existing description or comment fields without modification to the entire structure.

REVIEW OF OPDM'S ECONOMIC FORECASTING MODEL

In its facility plans, OPDM uses an economic forecasting model to compare the costs of straight leasing with several variations on lease-purchase and with bond financing. Consultants evaluated this forecasting model and, in general, it was found to be accurate, flexible, and useful. It is recommended that the model continue to be used, but with some clarifications of the definition of certain input variables. A summary of the process follows with a more complete discussion in Appendix E.

Consultants reviewed OPDM's Economic Forecasting Model (EFM) from a functional and technical perspective. The functional review assesses how the model is currently being used by OPDM and others in the office space decision-making process (both lease and build). The technical review includes an evaluation of the way in which the model variables interact, such as the calculation of 50-year bond financing costs. In addition to general structural considerations is an evaluation of the parameters OPDM currently uses for the model variables, such as bond interest rates and a discussion of how the accuracy of the model may be improved by changing some of these parameters.

Functional Review

The EFM is used as an analytical tool by OPDM to assist in office space financing decisions. Broadly speaking there are two general types of financing approaches used by OPDM to accommodate office needs that are incorporated in the EFM: Private and Public. The private options include straight leasing of privately-owned buildings and variations of lease/own, such as lease with an option to purchase and installment sale. The public

financing approaches use either capital outlay funds or a form of tax-exempt financing, such as lease revenue bonds or certificates of participation to raise money for constructing an office building. The EFM can evaluate the financing parameters within a single technique, such as straight leasing, or compare two different financing approaches, such as straight leasing vs. lease revenue bonds. Although it can be used to assist in leasing negotiations, the model is primarily used for OPDM planning purposes.

An economic forecasting model must be flexible to analyze, at different levels of detail, the economic trade-offs of private vs. public financing options at different points in the planning process. This means it must contain a sufficient number of variables that can interact to provide results at all stages of the process, from conceptual planning through working drawings. Consultants found that the number and types of variables included in the EFM were sufficient to carry out this mandate. Each of the different types of public and private financing approaches analyzed by the EFM contain this level of detail.

Technical Review

Consultants examined the structure of the model (i.e., the way it uses variables to determine the cost of private and public financing methods) to ascertain if it is appropriate for the analyses it is intended to perform. Like all models, results are only as good as the input assumptions used by the analyst. The input assumptions for the build option using tax-exempt financing were reviewed. Other input assumptions, such as operating and maintenance costs, construction costs and schedule, lease rates, etc., are beyond the scope of this study and were not reviewed.

Consultants generally found the technical aspects of the model to be acceptable. However, a few specific recommendations for changing the model are presented. The full technical review and recommendations are included in Appendix E; the following discussion presents only a brief summary of the analysis. (Please note this analysis does not lend itself well to summarization.)

- For purposes of the EFM, the arbitrage bond yield should be used for the debt serviced reserve, capitalized interest and construction fund for those projects with construction periods exceeding two years. If the project is certain to be built within two years, then a higher earnings rate could be used. For consistency purposes, the Pooled Money Investment Board's rate is recommended. This rate is used for the cost of a construction loan and the discount rate for comparing two alternative financing methods.
- The EFM can evaluate a multitude of financing options for space requirements, including private financing techniques such as straight

leasing, lease purchase option, installment sale and public techniques including lease revenue bonds and capital outlay funding. Because most of the DGS's office space needs are currently being met by straight leasing or new construction, if new buildings are constructed they are usually funded with lease revenue bonds. The EFM is used to determine the cost of financing new building with this technique. Variations to this funding method that are not currently being evaluated in the EFM, that can reduce the costs of bond financing, include a reduction or elimination of capitalized interest in lease revenue bonds and initiation of a Commercial Paper Program to reduce borrowing costs during construction. Consultants recommend these be considered in the EFM.

- Traditionally, bond financings for state office buildings have included capitalized interest payments during the construction period. Capitalized interest is required in lease financings because the lessee cannot begin rental payments supporting debt service until it has the beneficial use of the facility (which begins when it occupies the building). Consequently, the amount of money raised in bond proceeds includes the funds necessary to make interest-only payments during construction. The increased size of the bond issue increases the annual debt service payments and cost of financing.

The EFM analyst routinely uses capitalized interest in evaluating the cost of bond financing. However, asset substitution is recommended as an alternate approach. This financing alternative eliminates the need for capitalized interest. Asset substitution is described in more detail in the section on Financing Techniques.

Chapter 3

Reasons Why CAP Has Not Been Implemented

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REASONS WHY CAP HAS NOT BEEN IMPLEMENTED

This chapter sets forth seven major obstacles to the implementation of the Sacramento Facilities Plan. Consultants stress that these obstacles are all manifestations of the underlying reason: building offices has not been a priority for state decision makers. While some of these are more significant barriers than others, all can and have been overcome under the right circumstances. In a few recent instances (mostly outside of Sacramento), when buildings have been a priority, they have been built.

The state needs to decide if it still wishes to implement the Capitol Area and Sacramento Facilities Plans. If it does (or has only minor modifications), a clear commitment to do so is required. If not, an alternative plan is preferable to continuing on the present unguided course.

Below is a list of the seven reasons:

1. Decrease in Anticipated Sources of Capital Outlay Funding;
2. Limited Use of Alternative Sources of Funding;
3. No Effective Structure;
4. The Capital Outlay Process is Too Cumbersome;
5. No Pressure;
6. No Leadership;
7. Changed Conditions and Flawed Assumptions.

1. DECREASE IN ANTICIPATED SOURCES OF CAPITAL OUTLAY FUNDING

The most often stated reason for lack of implementation is "no money;" tidelands oil revenue has "dried up." The state government has traditionally acquired and built property through capital outlay funding. At the time of the Capitol Area Plan, it was assumed that such capital outlay funds would be appropriated from the General Fund. Several buildings were built in this way in the capitol area (Gregory Bateson, Water Resources Control Board or Paul Bonderson, Energy Commission, and Employment Development Department buildings). Shortly after the CAP was developed, however, Proposition 13 was passed by the voters. There was a sharp drop in revenues at the local level, yet the cities and counties were not able to reduce their expenditures proportionately. For a few years, the state was able to forestall fiscal crises by diverting part of its own surplus funds to the localities. As a consequence, the funds available for capital outlays were severely reduced. At the same time, there was a severe recession nationally, which reduced state tax revenues. The General Fund was no longer a good source for capital outlay.

Another potential source was found. Towards the end of the 1970s, California was receiving approximately \$400 million a year from tidelands oil revenues. A prescribed sequence of recipient funds was established to utilize these revenues. A certain amount of money would go to the first fund; when that level was reached, the second fund would be filled up and so on, rather like a series of buckets where each overflows into the next. None of these was large in comparison with the entire fund and when all the buckets were full, the balance would go into the Special Fund for Capital Outlay (SAFCO), which could be used for building. SAFCO funding for DGS capital projects was first proposed in the 1981-82 budget.

Through fiscal year (FY) 1986, the oil revenues were as anticipated, around \$500 million a year. Then, in 1986, as a result of oil prices, the oil income dropped precipitously to below \$200 million and has not recovered.

In order for any sort of funds to go into SAFCO, the sequencing process was bypassed and specific allocations "in lieu" were made to the various funds. In FY 1988-89, for example, SAFCO received \$82 million of the total of \$119 million in revenues. Most of the rest went to the State Lands Commission (operator of the offshore oil properties) and to the General Fund; this latter was designated for operating expenses rather than capital outlays.

The 1990-91 budget proposes \$82 million for SAFCO, \$14 million for the State Lands and \$20 million for the General Fund. This year's SAFCO funds are allocated among a number of small projects; the largest recipient is the Department of Mental Health. Oil revenues are not expected to rise in the immediate future; thus it seems that there will continue to be no substantial funds in SAFCO for the construction of large buildings.

It is significant to note that the end of capital outlay for constructing office buildings came a few years before the drying up of SAFCO funds, which did not occur until the 1985-86 fiscal year. Other construction projects, such as prisons, schools and water resources, held higher priority. Most of these were financed by general obligation bonds, but the emphasis appears to have "sent a signal" that office buildings were not a major priority.

2. LIMITED USE OF ALTERNATIVE SOURCES OF FUNDING

The state claims that it wishes to construct buildings in accordance with the CAP; and it also wants to use the cheapest means of funding (direct capital outlay). These two goals are incompatible. There is little prospect of obtaining capital outlay funding; either

alternative financing must be found or the facilities will not be built. Until the state acknowledges and accepts this elementary fact, the present inactivity will continue.

The excuse that "there is no money to pay for new space" is invalid. The state does have the money and is presently spending it, but on leasing rather than on construction. It has had only limited success in employing alternative means of financing which would cost only a little more than leasing even at the outset, and yet would lead to state ownership and great savings in the long run. CADA, the development authority originally conceived of precisely for the purpose of financing capital projects in the core area, has been involved only in housing and small-scale commercial development.

The limited use of alternatives can be expressed as a lack of imagination by the state in finding means to overcome the financial and other obstacles to building office space. However, the use of alternative means of financing is not a new concept for the state. Several of these were mentioned as far back as the original CAP in 1977. Problems with SAFCO were foreseen in the State of California Financing Alternatives, released in November, 1983, and a number of alternatives were discussed there also. Yet the state has, on occasion, shown the ability to overcome the financing impasse. The facilities built before 1983 were financed through direct capital outlay. Projects after that time (both in the capitol area and elsewhere) include the Public Utilities Commission building in San Francisco, the Franchise Tax Board Phases I and II, and the Ronald Reagan Building in Los Angeles. Slated to be built soon is the State Archives/Secretary of State's Office; the State Library is in process. All of these have employed some alternative form of financing.

For example, the Public Utilities Commission and Ronald Reagan buildings were built through a Joint Powers Authority and are being lease-purchased back. In Los Angeles, the funds for the working drawings were borrowed from the local redevelopment authority and repaid from revenue bonds issued by the JPA. The Franchise Tax Board Phase I construction was bid from the preliminary plans; the working drawings were included in the bid, and the contractor obtained financing privately. Then the state assumed and refinanced the construction loan (at lower interest, and with exemption from property taxes).

For Franchise Tax Board Phase II (FTB II), the State Archives and the State Library (which has not yet been approved by the governor) a new scheme has been adopted. Preliminary plans are funded through SAFCO; then in a single piece of legislation, DGS is authorized to borrow from the pooled money fund for the working drawings and then to issue revenue bonds both to repay the pooled fund and to finance

construction. For the FTB II and the Library, this scheme was adopted after several unsuccessful attempts to fund working drawings through SAFCO.

In short, alternative means are available and they work. The state has displayed considerable ingenuity in financing some of the facilities mentioned above. When it once again wishes to construct buildings in the Sacramento area, it will use funds already in hand or easily available to it.

3. NO EFFECTIVE STRUCTURE

There are three elements necessary for an effective organizational approach to planning and constructing buildings: planning, prioritizing and decision-making, and implementation. Major problems exist in the first two of these and are described below; implementation is discussed more briefly because most of the projects do not get that far.

Planning

The Office of Project Development and Management (OPDM) of the DGS is the unit designated to plan state office buildings in Sacramento and elsewhere in California. OPDM plans at several levels. It is charged with updating the Sacramento Facilities Plan, and it maintains a database containing information on the location, size, staffing and ownership of all office buildings in the Sacramento area. But a much larger amount of its time is spent in planning individual facilities or conducting sub-projects such as environmental and traffic, or siting and adjacency studies. In these cases, it does not initiate the study itself. It responds to, and is funded by, the requesting agency.

Consultants have reviewed OPDM's work at the Sacramento Facilities Plan level. Taking into consideration the resources available to them and their limited role in the process, Consultants find that they use professionally acceptable procedures and employ appropriate data and criteria.

More to the point is what is deficient in the planning structure. OPDM must simultaneously try to meet the needs of the overall Sacramento Facilities Plan and the desires of its client agencies, even when these do not coincide; it is not clear whose needs take precedence. The leasing of office space is handled not by OPDM but by OREDS. There is only now being developed (within OREDS) a database which includes nearly all of the state-owned land throughout California; OPDM has been hampered by not having access to a comprehensive and accurate source of data.

Within the present structural arrangement, OPDM can only react to other agencies' requests. It cannot initiate planning activity except at the very general level of the overall Sacramento Facilities Plan, and it cannot well integrate requests for leased space. Fragmented and incomplete responsibility means that systematic planning is inhibited.

Decision Making

Planning is a technical process. Setting the priorities on what is to be planned for and choosing among alternatives developed by planners are political activities since they involve transfer of resources, desirable locations, and prestige among competing agencies.

OPDM cannot perform this function. It is not isolated enough from the process to make impartial decisions, nor does it have the power to enforce of the decisions. There is no centralized high-level body with this responsibility. As a result, the priorities are set and the decisions made through informal political means. Each decision is made in view only of its advocates' needs without systematic input from the other concerned parties. Priority goes to those who seize it.

Whether or not such an erratic process is consistent with the democratic process overall is a question far beyond the scope of this study. What is clear is that it is not compatible with an orderly and rational planning process. Decisions are fragmented, politicized, and difficult to predict. When there is no identifiable central structure for determining what is to be bought, built, or leased, then the process can only proceed in an uncoordinated fashion quite at odds with the intent of the Capitol Area Plan.

Project Implementation

Both OPDM and the Office of the State Architect play roles in the actual building processes. OPDM guides building projects through the planning and development stages. OREDS acquires real estate as well as handling office space leasing. Responsibility is fragmented among these branches of DGS, the Department of Finance and the legislature whenever a step needs to be financed. Although in principle, legislation is required only two or three times (planning, architectural drawings, and construction), many projects do not turn out to be so simple. Complications anywhere in the process lead to annual budget reviews, with delays at each point.

The state makes decisions on the space acquisition process in an uncoordinated and piecemeal way. Since there is no central structure to plan, prioritize and construct new buildings or to rehabilitate older buildings, everything is made more cumbersome, more fractured, more difficult and more expensive. Projects that are accomplished may not be of

the most benefit to the state, the neighborhood, or the taxpayers. And anything that impedes the building process can only lead to further leasing and take the state further from the goals of the Capitol Area Plan.

4. CAPITAL OUTLAY PROCESS IS VERY CUMBERSOME

The Capital Outlay Budget Process (COBP) is the formalized process that the state uses to apportion funds for capital improvements. It contains numerous points of independent review in order to assure sound financial decisions. An understanding of the process and how it affects planning and policy decisions is necessary in evaluating the issues of financing and ownership versus leasing. The capital outlay process is very complex, requiring much persistence and dedication on the part of a department making the request for new space. The length of time required, monetary implications of that time, and problems associated with the various steps combine to make the process itself a significant obstacle.

Although the COBP is used for other facilities besides office space, this study addresses only its impact on the type of spaces covered in the Sacramento Facilities Plan. Ushering a project through the COBP is the responsibility of the agency making the request. DGS is frequently (but not necessarily) the requesting department for office space. In addition to the requesting agency, the Department of Finance, OPDM, the Office of the State Architect, OREDS, the governor, and the legislature all play significant roles in the COBP. Because all capital outlay planning is tied to the fiscal year, delay at any stage of the process is likely to have a domino effect on the timeline of a construction project, and on its budget.

Specific information is required for each step in the COBP. The Department of Finance and OPDM have prepared a detailed summary showing the requirements for the first phases. Consultants have, for review purposes, briefly summarized the information here. A more detailed description of each phase is included in Appendix B.

The capital outlay budget process consists of the following nine phases:

- Concept and Document
- Budget Package
- Land Acquisition
- Preliminary Plan
- Working Drawing
- Bidding
- Construction
- Claims and Close Out
- Environmental Review

Each of these phases is further broken down into specific activities that must be accomplished and approved before proceeding to the next phase. The complex chain of approvals and the need to adhere to schedules or fall behind a year are the principal reasons that it is an impediment to the building of state-owned space.

The full complexity of the statewide capital outlay process is grasped only when the potential statewide "loops" necessary to obtain funding for all phases of the construction process are included. Because the legislature approves many of the phases separately, usually in different budget years, and because of strict requirements on content, timing, and changes, the state capital outlay process can take many years longer than would be required for a private developer.

The estimated time to complete each step of the process has been estimated by the Department of General Services and the Department of Finance. According to these, the minimum time frame is under four years and the maximum is over nine years.

Consultants do not mean to imply that the COBP should be changed; only that the process is difficult and has the potential to add years to the amount of time it takes to complete a project.

The complexity of this process, when compared with the relative ease of leasing a building, is a factor that must be considered when analyzing why the state's goal of owning 90 percent of its office space has not been achieved.

5. NO PRESSURE

Constructing new space or even rehabilitating older buildings is a time-consuming, laborious and uncertain process. Obtaining space through leasing is far simpler and quicker. DGS' *Client Reference Guide*, in describing the procedures for requesting leasing assistance, indicates that OREDS needs about six months to complete simple lease renewals, and a year for renewals that are more complex such as those including provisions for significant revisions. New leases for buildings with less than 15,000 square feet (sq. ft.) require nine to twelve months, while for leases for buildings over 15,000 sq. ft., over twelve months is required. (A March, 1990 report by the Auditor General, The Department of General Services Needs to Improve Its Management of State Leases and Real Estate, summarizes these time frames. Even though that audit found that completing lease arrangements frequently took longer than the estimated time frames, the times were still far less than the seven to ten years needed to construct buildings.)

In addition, leased space in Sacramento is available and much less expensive than that in San Francisco or Los Angeles. Beginning around 1980, private developers seem to have anticipated the state's office needs, and have put up a number of buildings in the core area that conform to state requirements. This too makes leasing more attractive; what capital funds are available are diverted to the large cities where renting is almost prohibitive.

Because pressures caused by overcrowding can usually be relieved in a timely manner by leasing, agencies have little short-term reason to enter the complex and difficult process of capital improvements. The current practice of leasing rather than constructing has led to an enormous leasing program which will cost the state hundreds of millions of dollars in the long run.

6. NO LEADERSHIP

Despite the above factors, the state could, with effective leadership, find a way to build needed office buildings. However, legislative and executive priorities have concentrated on funding programs and corresponding staff increases without attending to the long-range physical location of programs and staff. Capital outlay funds have been diverted from office buildings to prisons, educational facilities and natural resources. This may be due in part to the fact that there is little constituency support for new state office buildings, and consequently, few public officials are willing to take the lead on such complex and visible projects. Office buildings are simply not a priority. While Consultants do not propose to examine the historical record of the period since 1983, it is clear that fulfilling the Sacramento Facilities Plan has not been a matter of great importance to the leadership of the state government. The facilities that have been built since then have not just "happened;" they have all had determined and influential individuals actively supporting them through the Department of Finance and the Governor's Office as well as the Legislative Analyst (and the legislature).

7. CHANGED CONDITIONS AND FLAWED ASSUMPTIONS

In addition to the previously listed financial and structural reasons, changes in conditions and assumptions of the original CAP have contributed to lack of implementation. One example is the goal of constructing large office buildings in the area north of "L" Street. The purpose of this was not so much to meet the state's needs as to give an economic impetus to a stagnating section of the city. Since then - indeed, by 1983 - private developers have constructed a number of large office buildings in this area. Whereas in 1977, it seemed that the decrease in tax revenues would be offset by the effect

of new construction, this is no longer the case. Construction has occurred without the state's intervention, and a revitalization program is no longer needed.

A second policy is the CAP's policy of development in the capitol area on quarter-block lots. This has proven to be an impractically small footprint, especially for parking structures, and there has been a shift to providing offices and housing on adjacent full blocks in order to preserve the spirit of the 24-hour mixed use concept.

A third is the changing environment of the central city. In the last few years, private developers have begun to construct large buildings along the south side of R Street. This area, which had been an industrial and warehouse district, is subject to local planning consideration, and future plans are uncertain.

Other conditions are still changing. Telecommuting can allow professionals and even some managers to work at home, on personal computers, or in satellite offices, as productively as if they came to the capitol area to work. Here is a potential for major savings: building size and cost; commuting time, gasoline and stress; and reduction in turnover (as with new mothers or those with mobility problems). Setting up a workable large-scale telecommuting program entails careful planning and control which has not yet been carried out. Consultants would only stress at this point that telecommuting deserves careful study and inclusion in future plans.

Finally, the CAP's original assumptions about transportation options were over-optimistic. Reliance on the automobile as transportation is far higher than the CAP's framers anticipated. It is highly unlikely that single-car ownership can be brought down to below the level of San Francisco, a city with almost five times the population density and far greater traffic and parking congestion than Sacramento will experience for decades.

None of these changed conditions or unrealistic assumptions should pose an insuperable barrier to implementation of the CAP. They mean only that certain details need to be revisited in order to bring it into alignment with current reality.

Chapter 4

Policy Analysis: Lease Vs. Own Issues

CHAPTER 4

POLICY ANALYSIS: LEASE VS. OWN ISSUES

This chapter examines the current policies relating to the state's lease vs. own decisions. It first presents the objectives, policies and actions set forth in the Capitol Area Plan and the Sacramento Facilities Plan, and discusses implementation of these policies. In the policy analysis, the advantages and disadvantages of different methods of acquiring space are first presented. Next, financial implications of the state's current practices are presented, and finally financial techniques that could be used to modify the state's current practices are suggested.

EXISTING POLICIES

The CAP sets forth the following objective for state office space.

"To provide offices and related services to meet present and future space requirements for the state of California near the state capitol and in the context of metropolitan Sacramento, in the most cost-effective manner."

The Sacramento Facilities Plan set forth the following policy to interpret the plan.

"Existing and future space requirements will be satisfied by leasing and acquiring new structures and/or rehabilitating existing office structures."

The specific action that was recommended was:

"Acquire approximately 90 percent and lease 10 percent of all office space required."

ALTERNATIVE MEANS OF ACQUIRING OFFICE SPACE

The alternative ways of acquiring office space are summarized below, followed by a list of advantages and disadvantages associated with each method.

- New buildings can be built by the state, with construction funds coming from capital outlay or through the sale of bonds.
- Space can be reclaimed in existing older buildings through rehabilitation, using the same types of funding.
- Existing privately-owned buildings can be purchased outright.
- Buildings can be acquired over time through lease-purchase or lease-option.
- Space can be leased in privately-owned buildings.

Space can be obtained in any of these ways. The uniqueness and variability of buildings, of owners, and of the real estate and financing markets guarantees that there will be no

single "right" choice under all circumstances. One of the most influential factors in choosing among alternative means of space acquisition is the financial implication. Although some of these options tend to be less expensive than others, under the right circumstances any one of them may be the most economical choice for the state.

Build

- Advantages:
- Building generally carries the lowest long-term costs of any option for equivalent new space. state-owned space is economical because the state has a low cost of capital, pays no property taxes, enjoys a low vacancy rate in its buildings, and requires no profit margin.
 - Building allows the state to select the design and location of new facilities as part of a coordinated long-term plan.
 - The state has direct control over the planners, architects, contractors, and maintenance. Special-use space can be incorporated into the design at the outset.
 - The state also has control over office environmental quality and energy conservation.
 - In Sacramento, state-owned land within the capitol area is available for office construction.
 - The state accumulates equity in a property which can later be sold if it is no longer useful.
 - Alterations and assignment of costs are simpler.
 - Building is generally accompanied by consolidation, which improves operational efficiency and decreases reliance on private transportation.
 - A visible permanent location can increase public identification and convenience.
- Disadvantages:
- The process is lengthy and laborious.
 - Construction by the state can be more expensive than if done by a private builder.
 - The cost of owned space is usually higher than that of leased space for the first few years.

Rehabilitate

- Advantages:
- Rehabilitation can be far cheaper than any other option.
 - The degree of consolidation is maintained or improved.
 - Public identification remains.
 - As with building, the state retains control and equity.
- Disadvantages:
- There are only a limited number of rehabilitation opportunities.
 - Only modest increases in floor area can be obtained.
 - Employees must be moved twice, out of the building temporarily and then back in again.

Purchase or Lease-Purchase

- Advantages:
- After the state obtains title, purchase or lease-purchase offer many of the same long-term advantages as construction, and two more:
 - Information on the suitability and condition of the building in its location is already available, especially if the state has been occupying it.
 - There are no moving costs.
- Disadvantages:
- The state does not have control over the building design. The building configuration may be less satisfactory than in a new building.
 - The state does not have control over the construction process. It cannot assure, for example, minority contractor participation, and may not easily be able to ascertain the degree of adherence to construction standards.
 - In lease-purchase, the short-term cost tends to be somewhat higher than in straight lease.

Straight Lease

- Advantages:
- This is the fastest and simplest way of obtaining space.
 - The space can be inspected before occupancy.
 - The initial cost is often lower than owning.
 - Leased space is flexible: it can best accommodate the needs of agencies with changing staff size.
- Disadvantages:
- In the long term, leasing tends to be the most expensive way of obtaining space.
 - As with purchased space, the state does not have control over the design or construction of the facility.
 - Leasing often leads to decentralization and dispersion, with their attendant disadvantages.
 - The state acquires no equity.
 - There are variable and sometimes unexpected costs in enforcing the terms of the lease.
 - Changes of ownership or bankruptcies cause additional problems.

FINANCIAL IMPLICATIONS OF THE CURRENT PRACTICES

One purpose of this study for the Auditor General is to determine whether it is cheaper to lease or build office space. The answer to this question is, unfortunately, "It depends." Determining the cost of leasing is not simple, and determining the cost of constructing an identical facility is extraordinarily dependent upon the assumptions made in the calculation and on external and uncontrollable market circumstances. There is no single universal answer.

The methodology used to address this issue stresses the conceptual nature of the analysis. There is no attempt to quantify the cost of lease vs own/build for all the office space the state currently rents and plans to rent or build in the future, as this is a major effort well beyond the scope of this study. However, an analytical approach to ascertaining lease vs. build costs is provided.

To compare the costs of straight leasing vs. constructing office buildings with tax-exempt lease financing two examples are used: a historical and hypothetical current analysis. Consultants have calculated the costs of financing and of leasing a 300,000 square-foot building in the Sacramento metropolitan area in 1978 and in 1990.

The calculation is complex, technical, and lengthy; it is presented in full in Appendix F. The results varied in magnitude but both models gave essentially the same picture.

The first model starts with a state-constructed building: the Division of Law Enforcement (DOJ), 4949 Broadway. The building was built through direct capital outlay, but the model calculates what it would have cost to finance the actual construction through lease-revenue bonds at the rates then available. These costs are then compared with what it would have cost to lease a building of the same size under the terms of a lease held on a different building (EDD) at that time. The second model is of a hypothetical building, again of the size of the DOJ facility, but using current Sacramento construction costs and lease rates.

The general approach was to develop annual costs for the lease vs. build options over a 50 year life of a "typical" Sacramento area building. The annual costs were evaluated at three points in time; the entire 50 year period, the first five years of occupancy, and the point at which the cost of leasing equaled the cost of building using tax-exempt bond financing (the break-even point).

The conceptual nature of the lease vs. build question is emphasized because of the large number of variables and assumptions that must be included to properly address the issue. These results are listed below and illustrated in Figure 1 and Figure 2.

Results

- a. In the long run, owning is far cheaper. In both the historical and hypothetical examples, over a 50-year building life, the cost to own a building is significantly less than straight leasing. The range of the savings, on a present value basis, for a 307,305 net square foot building is from \$17.5 to \$39.1

million. This is about \$0.35 to \$0.8 million per year or about \$1.14 to \$2.60 per net square foot per year.

- b. If the findings could be applied to the entire space currently leased in the Sacramento area (4,164,061 net square feet, 1988 Sacramento Facilities Plan, pg. vii), the savings (on a present value basis) over a 50-year period would range from \$4.7 to \$10.8 million per year.
- c. On the other hand, for the first decade or so the annual costs of leasing are lower. The difference is \$1 to \$3.8 million for the first four or five years; it then begins to decrease steadily. For these models the point where the annual ownership costs became less than leasing occurred between 14 and 17 years. The breakeven point for total accumulated cost fell between 24 and 34 years. By fifty years the leasing costs were several times the ownership costs and continuing to increase.
- d. If the state could realize these savings by leasing, rather than constructing, the buildings described in the Department of General Services' (DGS) 1989 Five Year Capital Plan, it would save \$3 to 6.8 million per year during that five-year period. But this savings does not consider the equity contributed by the state in the lease purchase option which is about \$6.6 million on a present value basis. (Leasing becomes more expensive over time because rents rise. Financing costs do not rise and bonds are paid off.)

Note: these costs are expressed as "present values;" that is, they slightly decrease future costs when compared with the present. This procedure, standard in financial analysis, takes into account the value of postponing the time of payment and makes it possible to compare expenses incurred at different times.

The figures provided in the results are intended to give the reader a sense of the order of magnitude of the costs associated with the lease vs. build question based on the conceptual analysis. They provide a basis for discussion of the issue, not an answer to the question. A much more detailed review of each existing state lease and potential leases the state may enter into, combined with specific cost information about new buildings, is necessary to begin to answer the build vs. lease question.

Figure 1
Lease versus Purchase Costs
Hypothetical Model

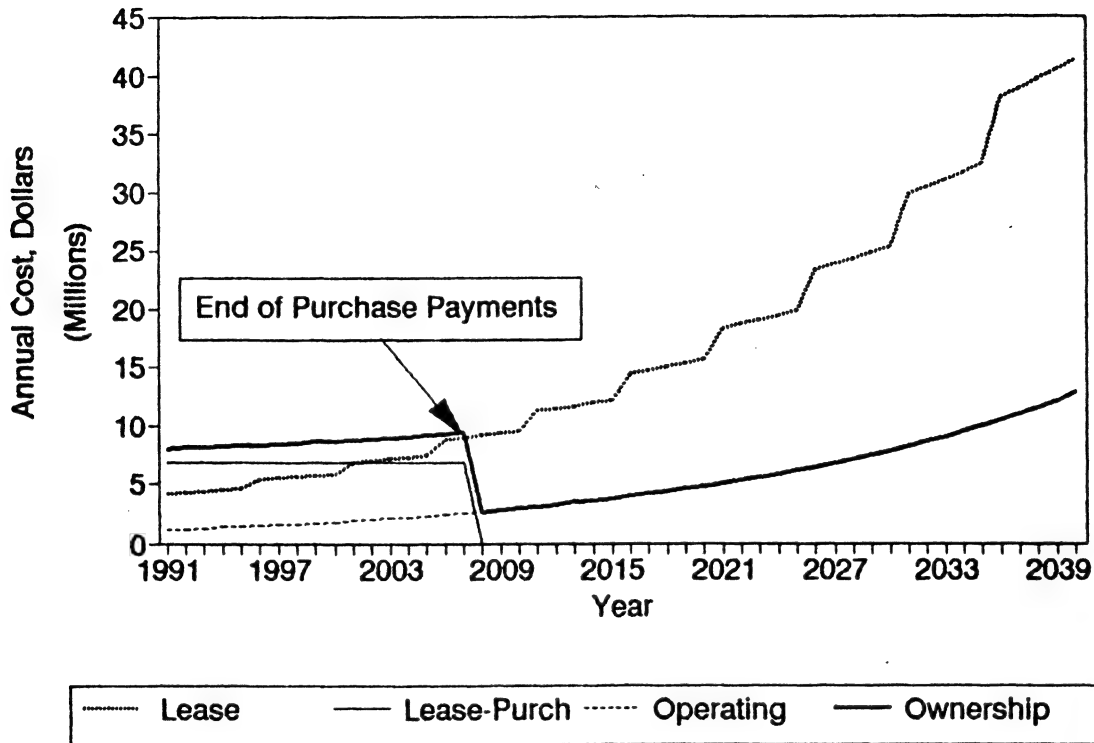
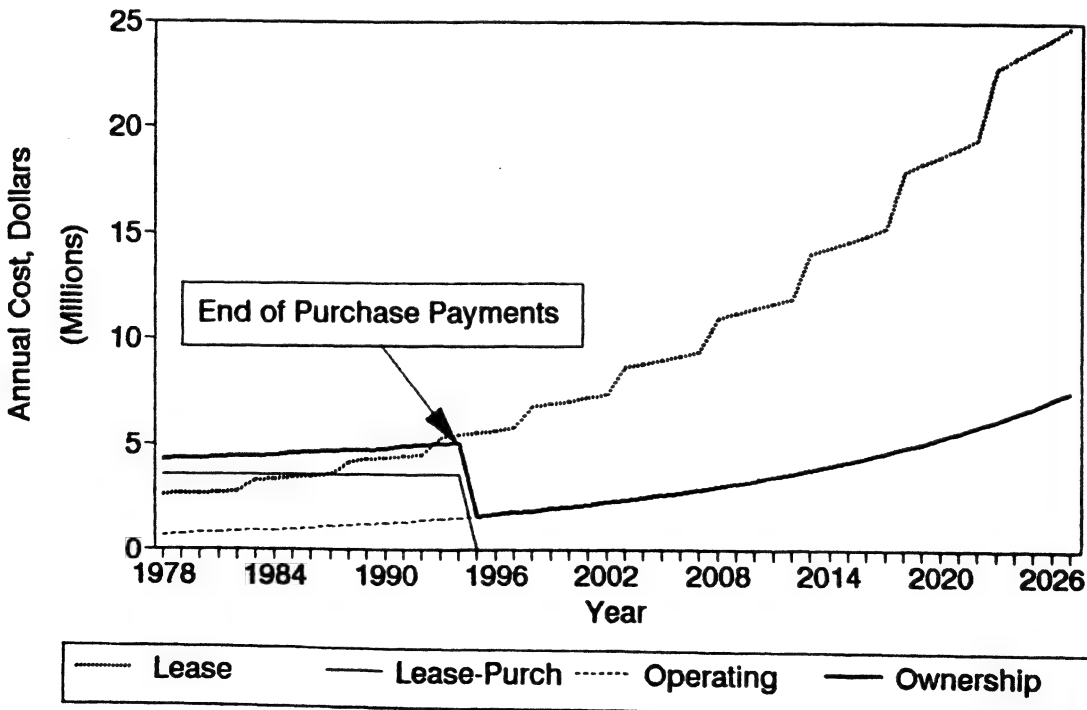


Figure 2
Lease versus Purchase Costs
Historical Model



Clearly the answer to the query "Is it cheaper to lease or build" depends not only on the myriad variables contained in the analysis, but on the time perspective. With a short-time horizon, it is cheaper to lease, not considering residual value. However, Consultants stress that because the state will have continuing needs for office facilities, it should adopt the long-term perspective. The payoff in owning its buildings would start to accrue to the state after 18 years or more, as shown in the Historical example, but this does not take into consideration the equity the state accumulates in offices it builds with lease revenue bond financing. Based on conceptual review, it appears that it is cheaper for the state to build and own its facilities.

FUNDING CHOICES

The state faces a paradoxical situation: to save more in the long run it must spend more in the short run. To financial analysts struggling desperately to balance this year's budget, achieving a savings only ten or fifteen years into the future must seem like an unaffordable luxury. Yet California will be here for the next fifty years, and many more. The state should take the long-range view in acquiring its facilities despite the attractiveness of short-term savings. It is peculiarly unfortunate that the time to break even after construction somewhat exceeds the normal tenure of most elected or appointed state officials.

Although Consultants recommend that the state build its office space with lease revenue bonds, the next issue to address is the ability of the state to issue bonds to raise capital to buy or build office buildings. What volume of lease-supported debt can the state support for its office construction program?

LEVELS OF LEASE-SUPPORTED DEBT

What level of lease revenue bond issuance can the state afford? To address this question, the general fund security for lease revenue bonds is briefly reviewed and then an integrated debt management process that would assist policy makers to determine the level of lease revenue bonds the state may consider for funding office construction is recommended.

In most state lease-supported debt structures, the underlying security for payment of debt service is the state's general fund. Lease payments are made from a department's annual general fund budget appropriation. The general fund, and a pledge of the state's full faith and credit, also secures the state's general obligation bonds. The level of lease-

supported bond issuance, therefore, is dependent on the issuance level of general obligation bonds, given the assumption that the state's policy is to maintain its AAA/AAA rating.

The guiding factors in determining the appropriate levels of general fund-supported debt (general obligation and lease-supported) are the economic, financial, and administrative criteria rating agencies use to rate municipal debt. These factors should be used in developing an integrated debt management model that assesses the impact of different proportions of additional general obligation and lease revenue bonds on the state's credit.³

Clearly, the overwhelming effect on the state's credit is the pace at which it sells its authorized bonds. Lease revenue bonds for new building construction will have a much smaller effect on certain rating agency criteria, such as net-debt per capita, but will become increasingly important in the ratio that measures lease-supported debt to gross-bonded debt. How can this information be used by DGS in its facilities planning process?

The State Treasurer's office is responsible for managing the state's debt. It analyzes the impact of proposed state borrowing, for all purposes and types of bonds, on the state's credit. As part of an integrated office facility planning process, the State Treasurer's office can provide DGS with maximum annual lease revenue bonding levels for its Five Year Capital Plan (and beyond) given the anticipated rate of general obligation bond issuance. DGS, in turn, would develop a priority process to allocate among its projects the allowable level of annual lease revenue bond proceeds determined by the Treasurer's office.

It was not possible in the scope of this study to obtain complete information about the Treasurer's office debt management process. The institutional framework for this information link between DGS and the Treasurer should be considered in the context of the overall DGS office facility planning process.

FINANCING TECHNIQUES

Despite its reluctance to abandon direct capital outlay funding, the state is by no means unaware of financing alternatives.

The Department of General Services and its consultants have, in several documents,

³See Appendix A for a brief description of the process used by the State of Maryland.

explained the financing techniques available for funding state office buildings.⁴ These techniques, which include both public and private financing categories, are presented in the flow chart on the following page. Because these various techniques have been described in detail in these previous reports, Consultants have focused on the two that appear to be the most useful to the state's needs. A complete explanation of these complex financing techniques is presented in Appendix G.

Consultants have reviewed the alternatives considered in the various documents associated with the plan, separating them broadly into the categories of public and private financing. Public financing implies public ownership and the use of tax-exempt bonds (or capital outlay) to finance construction. In private financing, a private party borrows the money and pays taxes on it while retaining ownership of the building, at least until the state assumes it.

Consultants recommend two modifications to the state's battery of financing methods. One is to continue the practice of using capital outlay to fund the plans and drawing phases of a project. The other is really a collection of short-range techniques to lower the cost of financing during the period of construction.

Private financing means that a taxable party, usually a developer (who pays federal, state and local taxes) is the owner of a building and provides his own equity and/or borrows in the taxable market to finance its construction. Once constructed, the developer negotiates with the state for use of the office space. The types of agreements the developer and the state may negotiate include leasing and lease-purchase arrangements.

Public financing implies public ownership and the use of tax-exempt borrowing and/or capital outlay funds to finance office construction.

Capital Outlay funds have traditionally funded the planning, design and construction of state office buildings. However, the availability of these funds for office

⁴a. State of California, Financing Alternatives State and Consumer Services Agency, Department of General Services, task Force on Alternative Financing, November, 1983.

b. Sacramento Facilities Plan, Eighth Supplement, July, 1988.

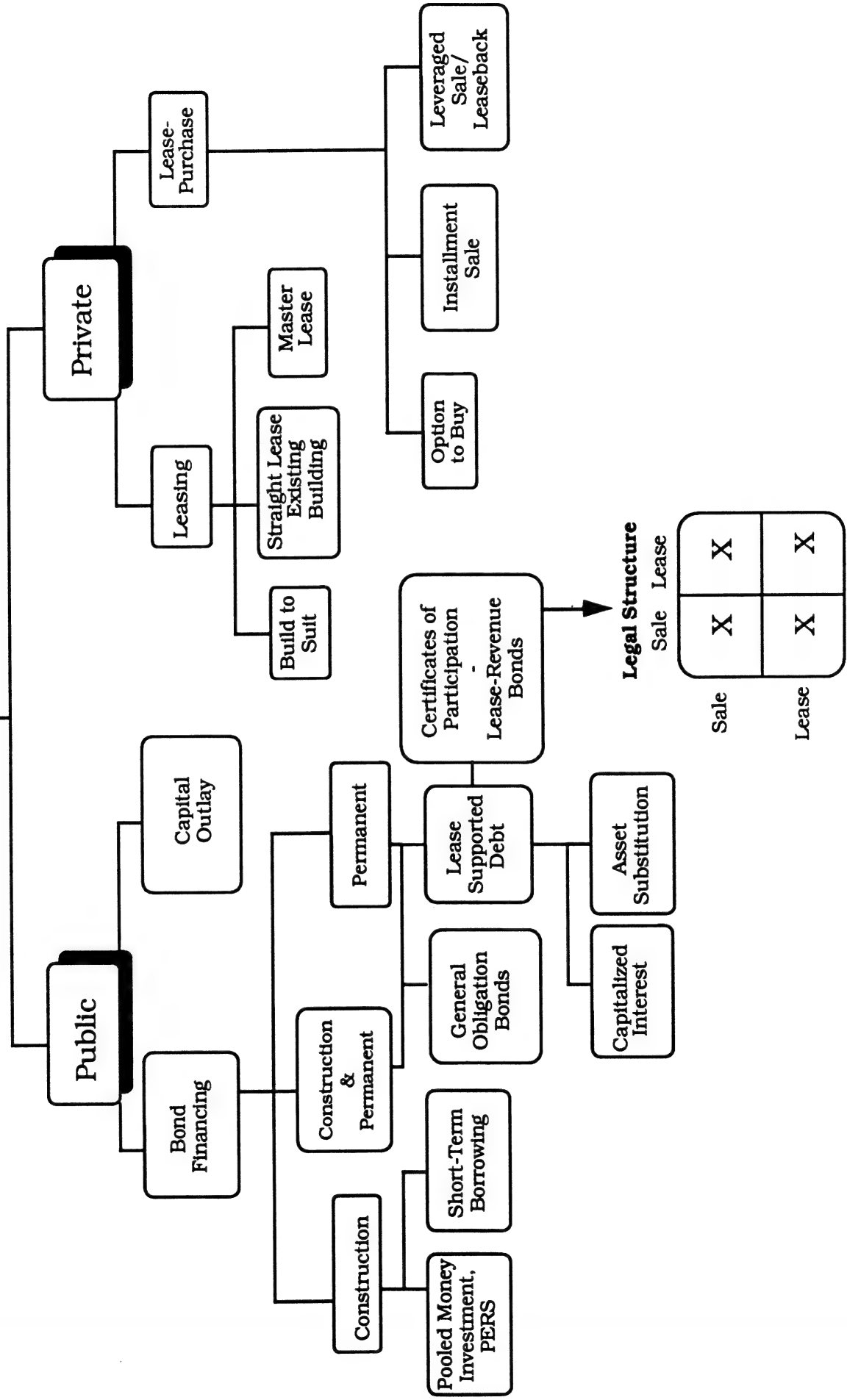
c. Deloitte, Haskins and Sells, State Property Management Demonstration Project, May, 1988.

d. Capitol Area Plan Progress Report, Office of Facilities Planning and Development, December, 1989.

e. Department of General Services, Five-Year Capital Outlay Program, September, 1989.

Financing Techniques

Flow Chart



construction has dramatically diminished because of Proposition 13, reduced tideland oil sales, and restriction of the use of Capital Outlay funds for the state's prison construction program and toxic waste cleanups. Because of this, Capital Outlay funds need to be used as efficiently as possible. Consultants recommend that capital outlay be used to fund all planning activities up until the time the legislature approves construction of a building. At this point other financing techniques can take over to finance working drawings (if this phase occurs after approval) and construction.

The state can use bonds/notes to fund the construction period, as a permanent loan, or for both construction and permanent financing for its office buildings. It typically uses one bond issue for construction and permanent financing, as was the case with the Ronald Reagan building in Los Angeles. However, financing options exist to split construction financing from permanent financing. In this case it has three ways to borrow money: from the Pooled Money Investment Board (PMIB), the Public Employees Retirement System (PERS), or with a short-term tax-exempt borrowing.

Borrowing from PMIB for construction and repaying the pool when it issues tax-exempt bonds, or borrowing from PERS are very costly approaches. The PMIB rate is a taxable money market rate that is 1.5 percent to 3.0 percent higher than a short-term tax-exempt rate. In addition, over 50 percent of the interest payments DGS makes on the PMIB loan benefits non-state municipal entities.

Borrowing in the short-term tax-exempt market could result in substantial savings over the construction period. The state can use either fixed or variable rate short-term borrowing to reduce construction costs. A fixed rate short-term borrowing would probably be at least 2.0 percent to 3.0 percent lower than the PMIB borrowing rate. The drawback of short-term financing is the risk of an increase in long-term rates at the time of the bond refinancing that could nullify any savings realized by the note borrowing.

A variable rate approach to short-term financing is a Commercial Paper Program. Commercial paper is a short-term tax-exempt borrowing instrument. It has a maturity of 1 to 270 days that can be structured to minimize interest expense. However, because of its short maturity the state would be exposed to a greater interest rate risk with commercial paper than with fixed rate short-term notes. Although this risk can be mitigated if the state is a frequent revenue bond borrower and expects to issue long-term bonds for construction projects on a regular basis, office buildings are built infrequently. A viable commercial paper program would most likely be established statewide and only if debt management policy allowed for variable interest rate risk.

The state can use general obligation bonds and lease-supported debt, either Certificates of Participation (COPS) or lease revenue bonds for construction and permanent financing. Given the current level of voter-authorized but unissued volume of general obligation debt, approximately \$12 billion, the legislature may not allow general obligation issues for office buildings to be placed on the ballot.

This leaves the lease-supported debt option. Certificates of participation and lease revenue bonds are the two most common forms of lease-backed municipal securities. In a COPS financing, investors purchase a share (participate in) of an underlying lease revenue stream paid by a municipal lessee to either a public, private or not-for profit lessor. Lease revenue bonds are similar to COPS, in that the underlying security for debt service payments are the lease payments by the public lessee. The selection of a COP or lease revenue bond legal structure depends on the statutory, institutional, political, economic and financial circumstances of the assets being financed.

Two financing techniques associated with lease-supported debt transactions are Capitalized Interest and Asset Substitution. In the capitalized interest approach, the state issues a single long-term lease revenue bond or COP, whose proceeds include an amount sufficient to pay interest on the bonds during the construction period. Lease payments cannot begin until construction is completed because the lease requires that the lessee have the beneficial use and occupancy of the facility. By capitalizing interest the state obviates the need for separate construction financing. But capitalizing interest is a costly way of constructing office buildings. Asset substitution can reduce or eliminate the need to capitalize interest.

Asset substitution is the replacement of a facility described in a lease that has not been built with the lease of a facility that has already been constructed. Bonds supported by lease payments on a constructed facility are sold, and the proceeds from the bond sale are used to build the proposed facility. The lessee can begin lease payments at the bond closing, rather than after the facility is constructed because it has the beneficial use and occupancy of the facility. Asset substitution also is known as an "equity strip". The state's financing of the Avenal Prison is an example of an asset substitution.⁵

⁵The 1988 Sacramento Facilities Plan describes an asset substitution for building rehabilitation projects (p. 34, #5). This concept can be expanded to include new buildings.

The State Public Works Board (PWB) issued \$104,000,000 of lease revenue bonds in 1985 to construct Avenal Prison. However, the lease supporting the transaction was not for the Avenal Prison, but the Southern Maximum Security Complex. The reason for the substitution was not to save capitalized interest expense, but because of a legal problem affecting the construction of the Avenal Prison. To affect the substitution the Southern Maximum Security Prison was effectively sold by the Department of Corrections for \$104,000,000 to the Public Works Board.⁶ The PWB sold lease revenue bonds to investors to pay for the purchase. The Department of Corrections leased the Complex back from the PWB and makes annual base rental payments equivalent to the debt service payments on the bonds. The proceeds from the bond sale were then used to construct the new Avenal Prison.

The substitution of the Maximum Security Complex in the lease for the unbuilt Avenal Prison saves the state money in two ways. First, the state does not pay capitalized interest, reducing bond size and annual debt service payments. Second, the state does not have construction completion risk for the leased facility. The Department of Corrections has the beneficial use and occupancy of the Southern Maximum Complex. Bondholders do not have to consider the risk of the facility not being completed on time so that lease payments can begin.

Asset substitution assumes that the appraised value of the building securing the lease is at least equivalent to the dollar amount of bond proceeds needed for constructing the new facility. If the state were to consider asset substitution for office and other lease-supported projects, then it should have a comprehensive list of unencumbered assets that can be used for substitution in lease financings.

Consultants recommend that the state should add to the Proactive Asset Management data base fields that includes the availability of the state assets for substitution in lease-revenue transactions. Depending on the state's policy regarding substitution, the data base should identify the unencumbered asset, its priority for substitution within the same department, and its availability for substitution with other departments.

⁶This is a general discussion of the legal structure. For a complete review of the legal structural aspects of the transaction, see the following bond documents: Bond Resolution; the Facility Lease Structural; and the Site Lease, \$104,000,000 State of Public Works Board of the State of California, Lease Revenue Bonds (Department of Corrections) 1985 Series A (Southern Maximum Security Complex).

Chapter 5

Policy Analysis: Consolidation and Location Issues

CHAPTER 5

POLICY ANALYSIS: CONSOLIDATION AND LOCATION ISSUES

INTRODUCTION AND DEFINITIONS

Both the Sacramento Facilities Plan and the CAP deal extensively with the policies of consolidation and location. These policies are not identical, but they overlap and interact substantially. For this reason they are often combined: the central concept of the Capitol Area Plan is the consolidation of state office space, locating it in the core area. These two issues also interact significantly with the ownership or leasing of a space.

Consolidation and location are for the most part discussed here together, but it is helpful to first separately define them as they will be distinguished at some points.

"Location" is simply where facilities are put in the Sacramento area. The terms "capitol area," "core area," "central city" and "metropolitan area" have specific meanings in the plan. The term "metropolitan area" will be used to indicate only parts of the Sacramento area outside of the capitol and core areas (which are bounded by 5th, G, 17th, and R Streets).

"Consolidation" is the process of bringing together agencies or departments into a single geographical planning area. (Dispersion is the opposite, defined as "scattered locations of agencies throughout the metropolitan area without regard to the interaction needs." This condition describes many of the state's agencies and offices today.)

The term "consolidation" has slightly different meanings in various contexts. While it always refers to the physical bringing together of previously separated units, it can be used at any level of organization and can be based on organizational or functional criteria. It can be the bringing together of departmental subdivisions that had become scattered through piecemeal leasing. It can bring together organizationally unrelated groups which have a high degree of interaction with each other; it can even refer to the placing together of noninteracting units which are too small to have an entire facility devoted to them.

An agency or department can be consolidated at two separate sites, say in the core area and in the metropolitan area. Finally, the degree of consolidation can vary: units may be placed in direct contact, on different floors, or in adjacent buildings. As the degree of consolidation decreases the advantages of consolidation decrease likewise.

If the only increase of office space were to be in the capitol area, then consolidation, location, and ownership would nearly coincide. The central theme of the Sacramento

Facilities Plan is to consolidate agencies into state-owned facilities located in the capitol area. Consolidation and location in the core will automatically occur when agencies move into these facilities.

Consolidation need not be in the core area. Agencies or departments can be consolidated in satellite campus-like office facilities in the central city or metropolitan Sacramento. The Division of Law Enforcement (DOJ), for example, consolidated several scattered units into a single large facility (4949 Broadway) outside of the central city. The Department of Motor Vehicles and the California Highway Patrol plan to share facilities at a number of locations statewide.

It is even possible to consolidate in leased space, especially if an entire building can be secured through a master lease. The Department of Corrections will be consolidated from several downtown locations into Benvenuti Plaza on R Street. But this is an exception to the general tendency that leasing increases dispersion and places the tenant agencies at less central locations.

CONSOLIDATION POLICIES

The Sacramento Facilities Plan was developed in order to determine who should locate downtown, who should remain in suburban locations, and the priority with which a department's needs are to be met. (CAP Office Element, pg. 12)

The following statements from the CAP, the CAP Office Element and the Sacramento Facilities Plan express the general intentions of the plan concerning consolidation. These policy statements present the overall intent and scope of the original plan, and provide a yardstick in measuring plan implementation.

"Consolidate state offices which are currently scattered throughout the metropolitan Sacramento by relocating those agencies that need to be downtown within a radius convenient to the capitol. This radius makes it logical to locate state-owned office space north of L Street, and about 1/3 of the new space will be located there. This consolidation will permit an improvement in the efficiency of operations now dispersed." ("Concept," Capitol Area Plan, pg. 4)"

The specific policies developed in support of rational, cost-effective office space were:

1. Reduction in the proportion of leased space to 10 percent
2. Location of new facilities within a ten-minute walking distance of the capitol.
3. Locating some state offices downtown north of "L."

4. "Develop a program to meet projected needs for state office space in the core area in a cost-efficient manner, including new construction of state-owned offices and rehabilitation of existing structures to office use."
5. Rehabilitating existing state office buildings to provide more efficient use of space. (p. 32.)

Policies promoting governmental consolidation are also reflected in state law: "Office operations housing more than 200 employees shall be within 1/4 mile of a public transit corridor." (Governmental Code 15808.1)

The Office Element of the CAP further specified consolidation criteria and an analytical framework for allocation and location of space. (p. 12-14.)

LOCATION POLICIES

The location policy in the 1977 Sacramento Facilities Plan was formulated to counter the impacts of dispersion of agencies and units in spatial and functional terms. This trend had developed as result of state population growth and attendant expansion in the size of state government, and a political preference in the prior administration for leasing office space rather than new construction.

The practice of leasing had the effect of dispersing governmental units throughout the metropolitan area since leasable space was found at various locations. This was magnified by the fact that the small floor plates of existing office stock could not accommodate the increasing size of most agencies; expansion led to further division.

The Sacramento Facilities Plan included the following criteria to use in deciding where to locate state agencies - either in the core area, or in the central city or metropolitan Sacramento.

Offices to be located in the core area include:

- Agencies with statewide functions;
- Agencies with functional and organizational relationships that require frequent face-to-face or mail communication;
- Agencies having organizational relationships with cabinet secretaries, constitutional officers, the governor, or the legislature, all of whom are in or near the capitol.

Offices to be located in the central city or metropolitan Sacramento are:

- Agencies with intensive space needs;
- Agencies whose functions relate to regional offices or field units;
- Agencies that serve clientele in specific geographic locations.

UNEXAMINED IMPLICATIONS OF THESE CRITERIA

Space in the core area is limited and valuable, and the block size is rather small. There is not room for all agencies meeting the core area locational criteria. Criterion number two says to locate "agencies with functional and organizational relationships with other entities that require frequent face-to-face or mail communication." It certainly makes sense to consolidate agencies with a high degree of interaction, but it does not necessarily follow that this needs to occur in the core area. It may be that agencies can be consolidated more easily elsewhere in the metropolitan area, and the advantages of consolidation can still be obtained.

Criterion number three is to locate in the core those agencies needing access to the governor or the legislature; the implication underlying it is that the agency as a whole needs such access. However, it may turn out that only the agency heads need to be downtown, and that the bulk of the employees could function just as well in a suburban location. The management may not even need to be near the capitol all the time. If this should be true it might suggest that alternate facilities might be built downtown for a small number of key staff - an "executive tower" - which could serve as a permanent, but part-time, second office for top personnel.

BENEFITS AND IMPACTS OF CONSOLIDATION AND LOCATION

Both the Sacramento Facilities Plan and the Capitol Area Plan discuss the benefits of consolidation. Consolidation of units that require contact with each other increases efficiency since interaction becomes easier. Consolidation allows sharing of facilities such as eating and break areas, conference rooms, lobbies, and reproduction. Energy conservation can be achieved through heating and cooling plan efficiencies.

A high density of employees can result in more use of mass transit or pooled transportation modes. Consolidation will also reduce interagency travel, which both saves staff time and reduces congestion and air pollution. If a new building is built for consolidation, financing costs can be reduced and special needs can be incorporated rather than being added on later at extra cost.

Dispersing state offices will have the opposite effects. Operating efficiency decreases; support facilities will be duplicated; automobile use rises and degrades air quality.

The effects of office locational decisions can be categorized into environmental impacts, traffic and transportation impacts, economic impacts, and social impacts.

Environmental and transportation impacts are closely linked, and the chief effect is on air quality. Other transportation impacts include traffic flow and congestion, parking, and the distribution of transportation among the various travel modes.

There is always a negative air and transportation impact at the location of a new building because there is always a local increase in traffic. However, this can be mitigated by careful design. More importantly, an increase in traffic at one location should decrease it at other locations. Severe bottlenecks may be broken up. Locating an agency near housing, as proposed in the CAP, will allow some employees to walk or bicycle to work and reduce total travel demand. The net effect of consolidation and strategic location on the traffic and air quality of the entire region should be positive if the transportation plan is well-conceived.

Large offices induce local economic growth; small (dispersed) offices have much less of an effect. If the new market is large enough, small businesses evolve to sell food, office supplies, and other retail products. The demand for local housing may increase. Then local property values and rents rise; this may force some existing tenants to relocate. When the state leases office space, the city of Sacramento realizes property tax revenues that would vanish if the buildings were state-owned; here the state and the city have opposing interests.

Not all agencies benefit in the same way from consolidation, or from locating in the core area. Special purpose facilities such as laboratories, rehabilitation centers, and correctional liaison centers tend to be incompatible with general office buildings because of the hazardous nature of their programs or the need for their clients to maintain a degree of anonymity.

Other factors opposing consolidation may include the necessity for an agency to serve a specific geographic area, a high level of public use which creates congestion problems, or a need to be identified with the community rather than with state government.

IMPLEMENTATION OF THE POLICIES

Since adoption of the plan in 1977 the amount of state office space in Sacramento has increased by 3.7 million NSF (net square feet). The projected demand over the next years is an additional 1.5 million NSF of office space.

Of this, a total of 1.7 million NSF in new state-owned construction was developed between 1977 and the early 1980s. The new buildings included four built within the core area and two in the metropolitan area. These buildings are:

Core Area

- Gregory Bateson
- Water Resources Control Board (Paul R. Bonderson)
- Energy Commission
- Employment Development Department

Metropolitan Area

- Department of Justice (4949 Broadway)
- Franchise Tax Board, Phase I (9645 Butterfield Way)

The last building to be constructed was the Franchise Tax Board, which was occupied in 1986. The FTB I project is part of a three-phase plan to consolidate this agency outside the core. Phase II is now in detailed design following a several year period where funds for drawings were denied.

Since adoption of the plan, the amount of leased office space has increased by more than 100 percent from 2.1 million NSF in 1977 to 4.2 million in 1988. About 1.3 million NSF was added in the period from 1980-1988. (Eighth Supplement p.13.). During this period leasing costs rose to their current level of \$55.5 million per year or \$4.6 million per month.

Seven years have elapsed since the state has begun construction of any new state-owned office facility. Since 1980 plans have been prepared for six buildings in Sacramento, but only the Franchise Tax Board Phase I was constructed. FTB Phase II and the State Archives project are now in the construction document phase and are slated for construction in 1991-1993.

The state has not carried out the location and consolidation study which systematically considers all the state agencies as proposed in the CAP Office Element. This kind of study would generate a matrix of agencies to be located and consolidated in specific planning areas.

ACTUAL OR EFFECTIVE POLICY ON CONSOLIDATION.

The real policy concerning consolidation is best understood by examining what has taken place since the plan was adopted. Plan implementation was a priority in the previous administration and a number of new buildings were built. In contrast, the state's need for office space since 1984 has been met through leasing. This practice has been followed despite numerous studies which demonstrate that new construction is, in most cases, the most cost effective long-term method to meet the demand for office space.

Decisions concerning office space and state construction are necessarily made in a political environment. The construction of large well-designed office buildings in the core area may invoke the image of wasteful big government and a leadership providing luxurious accommodations for pampered bureaucrats at taxpayer expense. Conversely, a policy based on no new construction and leasing private sector space may appear to be the essence of fiscal responsibility. This appearance masks the fact that leasing is not the most cost-effective long-term mechanism to meet office space needs, but results in a substantial additional annual cost to the taxpayers.

IMPACTS OF ACTUAL POLICY

Though there are some examples to the contrary, Consultants find that leasing has generally resulted in the continuing dispersion of agencies and offices throughout the metropolitan area. Consolidation of government offices in the core area may not be realizable through a policy largely dependent on leasing since the locations of large private sector buildings are based upon broader market considerations and may not be congruent with the CAP.

Continued primary dependence upon leasing will increase the dispersion of state agencies and offices. If lease rates within the core area accelerate beyond allowable state limits for Sacramento, the state can continue to raise its limits and thus its operating costs, or it can locate office space in smaller buildings in the metropolitan area. In the latter case, short term rental costs will again be minimized at the expense of long-term savings and the functional efficiencies associated with consolidation.

CHANGED / NEW CONDITIONS AND ASSUMPTIONS

Certain specific issues relevant to location and consolidation have arisen since the plans were written. One is the goal of constructing large office buildings in the area north of L Street. The purpose of this was not so much to meet the state's needs as to give an economic impetus to a stagnating section of the city. Since then--indeed, by 1983--private developers have constructed a number of large office buildings in this area. Whereas in 1977 it seemed that the decrease in tax revenues would be offset by the effect of new construction, this is no longer the case. Construction has occurred without the state's intervention and a revitalization program is no longer needed.

The plan called for development in the capitol area on quarter-block lots. This has proven to be an impractically small footprint, especially for parking structures. Providing

offices and housing on adjacent full blocks is suggested in order to preserve the spirit of the 24-hour mixed use concept.

In the last few years private developers have also begun to construct large buildings along the south side of R Street. This area, which had been an industrial and warehouse district, appears to be becoming a new locus of leasable office space. The plan did not anticipate these developments, but should now take note of them. In this area, however, there is a real need for improved communication between the city and the state as R Street developments will negatively impact the stable residential district just to the south.

The executive summary of the telecommuting pilot project, just completed for DGS, was made available for this study even though it has not yet been formally released. The study finds that professionals and even some managers can work at home, on personal computers, or (presumably) in satellite offices, as productively as if they came to work. Here is a potential for major savings: building size and cost; commuting time, gasoline, and stress; reduction in turnover (as with new mothers or those with mobility problems). However, the results are preliminary: setting up a workable large-scale telecommuting program entails careful planning and control which have not yet been carried out. Yet if telecommuting fulfills this early promise it deserves inclusion in future plans.

CONSOLIDATION CRITERIA

A methodology for analyzing consolidation needs was outlined in the Office Element of the Capitol Area Plan (April 1977, pp 12-14). This framework considered agencies and their interrelationships, zonal location, and allocation of new space to meet the objectives of consolidation and was to be used to determine which agencies should be consolidated in the core area. Although the Sacramento Facilities Plan provided this consolidation study, it may be worthwhile to examine these issues again, in a new consolidation study.

The revised consolidation study would serve as a guide to assure consistency in individual agency location decisions. In the absence of a guidance mechanism, short-term needs predominate and long-term needs and benefits are diminished or ignored. Incremental location decisions leave the state government without direction and the enduring perspective embodied in the Capitol Area Plan.

Another reason for a consolidation study is the fact that the core area is a bounded, scarce resource. An analysis in the Eighth Supplement demonstrates that it is not possible to meet all projected office demand in the core even if all new facilities on the sites

designated for offices are six stories in height (p. 29). Location within the area should be based on rational criteria rather than on agency preference or historical placement. Saturation of the core area will either cut off further expansion or require degradation of the CAP's density and mixed-use limitations.

When OPDM performs a study for a new facility it does so at the request of a given department. In the absence of a unified consolidation plan, it is limited to reacting to agency initiatives rather than proactively considering the overall evolution of the CAP. As DGS provides location assistance (either for leased space or for new buildings) the search will be focused only on the areas that have been identified as sites for the requesting agencies. If a systemwide study is used as a guide the state will examine all areas that are appropriate for consolidating state agencies.

This incremental approach represents a policy of random individual decisions which, in many cases, is further constrained by lease market conditions. It is a policy lacking in long-term vision and it inhibits the ability of DGS to provide office space which will "reduce expenditures and increase effectiveness."

Factors which should be considered in deciding whether an agency's operations should be consolidated or decentralized in Sacramento are discussed below. It is rare that any one of these factors will be decisive; their relative importance and impacts need to be weighed before the decision is made.

1. Organizational Structure of Agencies

Functional relationships within the department would be improved by consolidation because contact is facilitated.

2. Demand for Consolidation

Consolidation of state agencies into multi-tenant state-owned office buildings from dispersed leased facilities would result in substantial program savings, transportation cost savings, energy savings, and facility financing cost savings.

3. Linkage to Executive or Legislative Activities

Agencies that need to interact with the governor or legislature should be located near the capitol and legislative office facilities. A comprehensive survey of agency interaction patterns would permit the most rational setting of priorities on agency location in the core area. Some agencies which are now in the core area may no longer require location there.

4. Degree of Interaction among Agencies

Agencies with a high degree of interaction should be located close to each other. One example is the co-location of the Treasurer, the Controller and the Board of Equalization within the core area. Another example is the current location of the headquarters of the Highway Patrol and the Department of Motor Vehicles on the same site in the metropolitan zone.

5. Agency Size and Projected Growth

The efficiency of current space usage, evaluated in terms of staff and building size, storage, requirements for data processing, and other uses, and projected space allocation plans for five and ten years will indicate whether an agency should remain in its present location. Factors influencing the public demand for the agency's services should be taken into account. Space usage greatly at variance with space needs requires reevaluation.

6. Adequacy and Quality of Space

Standards for spatial requirements, environmental conditions and building systems efficiency should be used to assess the adequacy and quality of both state-owned buildings and leased facilities, in particular the older state-owned office buildings. The need for new buildings increases where the existing facilities are substandard and it is not economically feasible to refurbish them.

7. Economic Benefits & Costs

Each proposed consolidation scheme should be studied to determine savings in program costs, transportation, energy, and financing costs.

8. Population Served

Agencies having a high degree of direct interaction with the public should be located to facilitate access. If a local clientele is served the responsible unit should be in a convenient location. It may be found that the management and central administration of an agency should be located in the core and that units serving the Sacramento area only are best placed in the periphery, especially when the central and local units do not require daily contact.

9. Transportation

Consolidation to readily accessible centrally located, consolidated office buildings meets the transportation goals of the state by reducing the total vehicle miles traveled by consolidating from many locations into one location, encourages the use of public transit by

locating the facilities on public transit routes, and encourages carpools by limiting the on-site parking.

10. Availability of Sites

Are there sites that are readily available to the state for office development? In those proposed office building areas where the state either owns building sites or sites are readily available, staging of an office building project can be implemented within a shorter time frame.

11. Availability of Comparable Leased Space

Is there enough space in the private sector to permit growth and expansion? Are those facilities adequate? Do they otherwise conform to the CAP requirements?

12. Benefits to the Local Community

It would seem reasonable for the state to locate its office buildings in those areas where the greatest socioeconomic benefits will result to the local community. Although choosing to consolidate in state-owned buildings may adversely impact local real estate developers when they lose their tenants, it will benefit local construction companies who build the new state office buildings. In the long term, the service industries of a neighborhood are enhanced by the relocation of state employees into the area.

13. Compatibility with State and Local Planning

Although the state plans primarily for its own benefit, it is important that it work with local government in the selection of sites for state office buildings. The state should recommend office building sites which are consistent with local planning goals and land use.

RECOMMENDATIONS

The state should conduct a systemwide location and consolidation study including all state agencies that will become the basis of all future location decisions.

The plan for consolidation and location should be based on the overall benefit to the state, not merely agency preference. Included in this should be agencies currently housed in the core as well as those in leased space or housed in the metropolitan area.

The state should develop a leasing policy which fits the results of the consolidation study. This suggests that the short-run leasing activities of the state should as much as possible conform with the locations identified as prime sites for future consolidation.

The state should consider locating and consolidating compatible agencies with complementary functions and a high degree of interaction in a master planned campus-like office setting in metropolitan Sacramento.

Chapter 6

Policy Analysis: Public Benefit Issues

CHAPTER 6

POLICY ANALYSIS: PUBLIC BENEFIT ISSUES

This chapter discusses the public benefits resulting from state actions and decisions. These public benefits should be measured in terms of positive and negative impact to the citizens of the state of California overall, and to the Sacramento area.

One of the most important public benefits is simply the cost savings derived from specific actions or decisions. The determination of the relative costs of building versus leasing office space, and of the most beneficial method of financing, was discussed in detail in Chapter Four. As discussed there, Consultants believe that Public Benefit must consider the long-term cost to the state, and that building is preferable to leasing.

Another policy area with substantial impact on the financial benefits is rehabilitation of existing structure. A more complete discussion will be presented in Chapter 7.

Another major public benefit is based on how location and consolidation issues negatively and positively impact on the Sacramento area. While the issues of consolidation were discussed in some detail in Chapter Five, specific impacts of those policies are explored in more detail in this chapter. These include impact on the environment, parking and transportation issues, infrastructure, child care.

TRANSPORTATION IMPACTS

Quarter Block Concept

The application of the quarter-block concept, which is based on the policy that new state office buildings would be a quarter block in size and scale, provides a significant constraint on the ability to provide adequate parking facilities. The concept limits flexibility in garage design, restricts the location of garage access points, and often creates operational deficiencies. This can result in higher garage costs and impacts on adjacent downtown streets.

The use of the quarter-block concept limits the number of garage design options that are available based on the small area of the resulting parcel. For example, the effective size of a quarter block in the downtown area is typically 160 feet by 160 feet or less. The sloping floor garage design is generally the most efficient as the floors serve both as aisles and parking bays. It is difficult to design a garage with sloping floors on a quarter-block parcel, however, due to limits in floor grades on which vehicles may be parked. As a result, the garages may require a separate ramp system to provide access to each parking

level. This reduces the total amount of structured area available for parking bays, resulting in greater construction costs per stall.

The location of a garage driveway affects the need for queuing space (e.g., the stacking of vehicles waiting to exit or enter) both within the garage and on the adjacent public street. The quarter block concept limits the location of the garage access to the mid-block end of the garage to avoid congestion at the adjacent intersection. The placement of the garage access at the edge of the garage further limits the design options and can create a circulation bottleneck if not carefully controlled.

Implications of Telecommuting

The potential impact of telecommuting on parking demand in the downtown area is difficult to define as there is limited data available on this concept. In addition, the effect of telecommuting on office needs and parking demand varies substantially depending on whether work is performed at home or in satellite offices.

As the state is currently involved in a pilot program for telecommuting that involves approximately 200 employees, additional information should be gathered on the results of the program and applicability of telecommuting for state employees in the downtown area.

If telecommuting were achieved through the implementation of satellite offices, it would represent in effect a decentralization of state office into the suburban areas. Since the demand for office space is based on the estimated number of employees for each agency, decentralization would require that an equivalent level of office space be leased or constructed by the state. The following issues should be addressed in any assessment of decentralization.

- If a significant level of office space were constructed in the suburbs, transit service would have to be expanded to provide inter-suburb commuter service.
- The development of suburb office space typically results in a higher demand for parking due to the limited transit service and lower land costs.
- The development of suburb office space would result in localized traffic impacts that may be significant.
- Telecommuting could result in a reduction in the demand for future office space if work was performed in home offices. Further study is necessary, however, to indicate what proportion of state office workers are candidates for telecommuting, what effect it would have on management techniques, and whether a part-time presence by employees at a primary office would be required.

Public Transit Goals

Surveys of state employees conducted in 1988 indicated that approximately 23 percent traveled to work by public transit. This included 12 percent by light rail, six percent by standard buses, and five percent by shuttle buses. This is slightly lower than the level of transit ridership experienced in 1975, when 27 percent of state employees traveled to work by bus. These levels of transit use are substantially lower than the goal established for the year 2000, when 50 percent of state employees are projected to travel by public transit.

The year 2000 goals for reducing the number of automobiles traveling to the capitol area will be very difficult to achieve without significant changes in travel patterns. Currently, approximately 71 percent of state employees travel to the downtown area by automobile. This is one-half the goal of 35 percent established for the year 2000.

A review of travel characteristics of downtown employees in San Francisco, Los Angeles, and San Diego indicate that the travel goals for downtown Sacramento in the year 2000 would result in lower proportions of single-occupant automobiles than these other three metropolitan areas. This does not appear to be a likely scenario based on current trends in downtown Sacramento. Table 1 shows a comparison of existing travel mode splits for the four cities listed above.

The transportation impacts of not meeting the commute goals that have been established for state employees in the downtown area are increased congestion and a greater demand for parking. The 1977 Capitol Area Plan calls for the development of 12,020 parking spaces by the year 2000 to accommodate state office employees and visitors, based on the commute goals. If the current commute trends continue and the projection of 32,900 employees is accurate, the state would experience a shortfall of approximately 8,900 parking spaces by the year 2000. A 30 percent reduction in the current level of automobile ridership would result in a shortfall of approximately 3,400 parking spaces.

Table 1
Employee Commute Patterns

Commute Method	San Francisco	Los Angeles	San Diego	Sacramento Now	Sacramento Yr 2000 Goal
Drive Alone	10.5%	60%	51%	41%	5%
Carpool Driver	4.2%	3%	17%	14%	11%
Auto Passenger	6.3%	14%	25%	16%	19%
Bus/Rail	73%	21%	7%	24%	50%
Walk	4.1%	2%	-	1%	5%
Motorcycle	0.6%	-	-	1%	4%
Bike	-	-	-	3%	6%

Peripheral Parking Facilities

The shuttle buses provided for peripheral parking lots are currently used by approximately five percent of state employees. This is much lower than the goal of 23 percent that has been established for the year 2000. The lower demand for peripheral parking has also been documented through surveys of the lots that indicate they are underutilized in comparison to parking facilities in the core area. As the desired demand levels for a parking garage should not exceed 90 percent of the supply, the occupancy rate of 77 percent experienced in the peripheral lots indicates that there is sufficient capacity to accommodate an additional 200 vehicles.

Additional parking facilities will be necessary to accommodate the desired increase in demand for peripheral lots. As stated above, the current supply of 1,469 spaces provides a reserve of approximately 200 stalls. The year 2000 goal for the downtown area is the provision of 5,300 parking stalls in peripheral lots. This would require the construction of an additional 2,831 stalls over the next ten years.

Several factors affect the relative use of these peripheral lots. The monthly fees for these parking facilities are only slightly lower than those of core area garages. In addition, there is a need to transfer beyond a reasonable walking distance. As such, the development of an incentive program is recommended to ensure the utilization of additional peripheral lots as further construction occurs in the core area. This would include the provision of economic incentives (i.e., subsidized parking fees) and a highly visible shuttle service.

ENVIRONMENTAL IMPACTS

The complex process of building or renovating state office space in the capitol area is further complicated by the California Environmental Quality Act (CEQA) requirements.⁷ CEQA guidelines call for an environmental impact report (EIR) to be written when a construction project may involve impacts on the surrounding environment. Most, if not all, such projects in the capitol area would require an EIR.

After the CAP was written in 1977, the 1977 Capitol Area Plan Final Environmental Impact Report (CAP FEIR) was published. The CAP FEIR's principal objective was to inform public decision makers and the general public about the possible environmental effects of the policies contained within the CAP. Because the CAP is a master plan and thus a policy document, the CAP FEIR is deliberately general and primarily limited to policy considerations as they may affect the environment. It was intended that subsequent environmental documents would address incremental planning efforts for projects pursuant to CEQA guidelines.⁸

Since its publication in 1977, the CAP FEIR has not been revised. The actual environmental conditions of the capitol and adjacent areas have changed, making much of the information contained in the CAP FEIR outdated.

DGS does not plan to update the CAP FEIR until 1) there is more information regarding local government plans; 2) the state is able to identify a reasonable target for ownership versus leased office space; and 3) outstanding questions in the CAP supplement are addressed.

Project-specific environmental impact reports (EIR) continue to occur, however. The EIR process has sometimes hampered the process of construction. One problem is that because of the length of time that it often takes to get a project finalized, environmental changes, particularly cumulative ones, may have occurred which may outdate some areas addressed in the project EIR. Other problems involve the assessment of cumulative effects and mitigation measures. Assessment of mitigation fees has the potential for being an ongoing problem. One approach to this problem is legislation that establishes an account in the State Treasurer's office. This account would be made up of accrued revenues for fees for mitigation monitoring and costs.

⁷Consultants do not mean to imply that adhering to CEQA requirements is undesirable. In fact, Consultants are in favor of careful environmental analysis.

⁸California Department of General Services. Capitol Area Plan Environmental Impact Report, 1977, p. 1-2.

CHILD CARE IMPACTS

Government Code Section 4560 mandates that all newly constructed state-owned buildings, or those altered more than 25 percent which can accommodate 700 or more state employees must designate space for child care facilities.

OPDM has interpreted this to include buildings funded by sale of revenue bonds or certificates of participation under lease purchase agreements. If either of these accommodate more than 700 employees, child care facilities are required.

While space for child care facilities is mandated, further assistance from the state in getting child care facilities started is quite limited. As this is a new program, data is quite limited in terms of the effectiveness of the spaces, and the criteria and guidelines that should be followed. Further information is required that will address feasibility and benefits of various sizes of facilities and their location. Considerable follow-up information will have to be gathered to address these issues.

One additional planning issue concerns the impact of child care on the tax-exempt status of bonds. If greater than ten percent of space in a state-owned building benefits private parties, the bonds may not be considered as public purpose, tax-exempt bonds. If cafeterias, concessions and child care facilities in the building are privately occupied, the square footage occupied and the cost of building the facility for private purposes need to be carefully explored.

ENERGY EFFICIENCY IMPACTS

The Sacramento Facilities Plan includes a policy to address the energy resources used by the state. This policy directed the state to, "Set into action a prompt and serious commitment to the efficient use of energy, including immediate development of renewable energy resources in the Sacramento area."

Specific actions that were recommended, including energy audits, recycling programs, alternative sources of energy, design criteria, minimizing energy expended in transportation and alternative transit modes. The actions that deal directly with transportation have been discussed earlier in the transportation section of this chapter. Consultants did not conduct an extensive policy review of other suggested actions. Need for considering these issues is relevant primarily when construction or rehabilitation occurs. However, as in other areas, Consultants believe that implementation is hampered by a lack of data.

Buildings that were constructed using alternative energy have not been analyzed for effectiveness. Such an analysis should take into account not only energy savings, but long- and short-term cost effectiveness. Assessment should also take into account how successful these buildings are in providing spaces that are conducive to efficient office workers.

This information should be included as the state makes decisions on future design of new buildings and rehabilitation of older ones.

Chapter 7

Policy Analysis: Older Office Building Restoration Issues

CHAPTER 7

POLICY ANALYSIS: OLDER OFFICE BUILDING RESTORATION ISSUES

This chapter analyzes state policies, procedures and actions relative to older state office buildings in Sacramento. Issues raised in the Eighth Supplement (restoration feasibility, asbestos abatement, special repairs and historic preservation) are discussed, and are followed by recommendations.

This issue is important because the state currently owns 3.2 million net square feet (NSF) of office space in Sacramento over twenty years old. These facilities, primarily located in the core area, comprise 62 percent of current state-owned office stock (5.26 million NSF) in the capitol area (eighteen office buildings in the core area and four in the metropolitan area). Thirteen buildings within the core area are over 40,000 net square feet in area. Among this group, seven structures (55% of state-owned offices) were constructed before 1940.

Table 2
State Owned Office Buildings in Sacramento Over Twenty Years Old
40,000 NSF or larger

	Year Built	NSF
Core Area		
Capitol Mall(Unruh)	1925	110,484
914 Capitol Mall (Lib & Cts)	1928	74,660
1020N/1021 O (Consumer Affairs)	1937	190,000
1120 N (Caltrans)	1936	300,650
1220 N/1215 O (Food & Ag)	1936	147,000
1025 P (Franchise Tax)	1927	94,287
1227 O (Vets Affairs)	1957	110,000
1020 O (Archives)	1922	42,555
1416-9th(Resources)	1965	488,642
714/744 P (Health Services)	1969	407,770
721 Capitol Mall(Education)	1953	103,745
800 Capitol Mall(EDD)	1955	345,900
801 Capitol Mall (SPB)	1955	54,450
Metropolitan Area		
2415-1st/2570-24th(DMV)	1964	607,838
2490-1st/2555-1st (CHP)	n/a	78,355

(Source: Sacramento Facilities Plan Eighth Supplement, 1988, p. 31.)

The older state office buildings above represent a valuable governmental resource. Replacement cost of these buildings in 1990 dollars would be at least \$440 million, assuming 20 percent grossing increment (for circulation and mechanics, etc.) at a current

office construction cost of \$115 per square foot, and land and project development costs would add significantly to this figure.

STATE POLICIES ON OLDER OFFICE BUILDINGS IN SACRAMENTO

The importance of maintaining and upgrading the state's older Sacramento facilities has been recognized in policy statements since the inception of the CAP in 1977, and updates have continued to emphasize the need for improving conditions in these buildings. Policies and recommendations that are especially relevant to the remodeling issue include:

- "Develop a program to meet projected needs for state office space in the core area in a cost-efficient manner, including new construction of state-owned offices and rehabilitation of existing structures to office use." (1977 CAP Office Element, Policy 4)
- "Rehabilitate existing office buildings to provide more efficient use of space, with attention to energy use, safety, aesthetics, employee work environment, and access for the handicapped." (1977 CAP Office Element, Policy 5)
- "Existing state-owned office buildings are a resource which need funding for adequate maintenance, and in some cases extensive rehabilitation to provide more efficient, safe, productive and pleasant workplaces. Making the best use of these existing resources should be made a first priority of the state's building program, ahead of the construction of new buildings." (A recommendation in CAP Progress Report, Dec. 1989, p. 47)

The Eighth Supplement affirmed the original CAP policies but raised significant issues which would prevent plan implementation. The specific implementation issues are:

- What is the economic feasibility of restoring older office buildings in light of costs for correction of hazards and upgrading?
- Why have special building repairs been only partially funded?
- What potential cost does asbestos abatement represent?
- As historical resources, what additional restrictions are older buildings containing asbestos subject to?

Since 1977 only one of the twenty-two older state office buildings in Sacramento has proceeded with a major rehabilitation project.

None of the twenty-two older state-owned buildings in Sacramento has undergone major renovation since development of the Capitol Area Plan in 1977; the Veteran's Affairs Building is scheduled for upgrade.

The most recent DGS Five Year Capital Outlay Program includes requests for twenty-four projects. The first five projects are for major renovation (seismic safety, economics, fire/life safety) of state office buildings which were damaged in the October, 1989 earthquake. There are no requests for Sacramento's older state office space.

Consultants believe that reasons for this lack of implementation are basically the same as with construction of buildings. In addition, responsibility for planning and carrying out rehabilitation is shared by OPDM, OREDS, OSA and the Office of Buildings and Grounds. Tenant agencies also contribute to the decision-making process.

There is a need to streamline the major projects' budget and planning process with respect to older state office buildings. Maintenance and office modernization are central components in implementing the state's policy to "Rehabilitate existing office buildings to provide more efficient use of space, with attention to energy use, safety, aesthetics, employee work environment, and access for the handicapped." Lack of capital outlay funds has resulted in minimal upgrading of the existing older office stock.

ECONOMIC FEASIBILITY OF RESTORATION

The feasibility of restoring buildings must be determined on a case-by-case basis. The process is singularly dependent upon critical analyses of structure, fire and life safety, and other factors. Restoration feasibility is idiosyncratic, and it is extremely difficult to estimate costs and to model or generalize costs from one project to another.

Only two buildings in the core area have been studied at a level of detail to determine the feasibility of restoration. These buildings, the Franchise Tax Building (1025 P) and the Archives (1020 O), were evaluated for their reuse potential as part of the Secretary of State and Archives project. The studies concluded that these older facilities (1922, 1927) should be demolished to permit efficient and cost-effective development of the new project (Site 7).

OSA has also prepared detailed "infrastructure studies" of the State Office Building in Oakland, and the three state-owned facilities in San Francisco. These studies, which were prepared before the October, 1989 Loma Prieta earthquake, provided a detailed comprehensive assessment of each building and served as the basis for the first priority requests in the most recent DGS Five Year Capital Outlay Plan. Each "infrastructure study" is a complete review of the conditions within an existing building. Elements include structural analyses, fire and life safety analyses, evaluations of mechanical systems, and functional and environmental conditions. Handicapped accessibility and historical preservation issues were also studied.

However, completed studies have been driven by the demand from tenant agencies, rather than part of a strategic approach to these building resources. Neither OPDM nor OSA has sufficient data to make a systematic determination as to the cost or feasibility of

restoring all of the older office buildings in the capitol area. In the absence of a detailed study of each of the state's older office buildings it is not possible to comprehensively determine the feasibility of restoration of the older state-owned office buildings. Questions pertaining to asbestos, for example, cannot be considered in isolation; they must be evaluated in light of a range of concerns including seismic resistance, fire and life safety, function, environment, site size and location.

Detailed "infrastructure studies" are needed to make rational, cost-effective decisions relative to restoration feasibility and to plan for the core area in a more holistic manner. (It should be noted that the DGS proposed a detailed study of the Unruh Building for cost of \$150,000. This request was denied by the legislature.)

Consultants conducted a case study comparing the current Veteran's Affairs Building rehabilitation project with a theoretical example of replacement on a new site. The case study is set forth below and illustrates the need to study every building in detail as part of the feasibility process. It also illustrates that, in some cases, rehabilitation is a viable alternative to replacement.

The planning and design process for the Veteran's Affairs Building has taken four years and has involved staff from Veteran's Affairs, OPDM, OREDS, and OSA, as well as a consultant team including architects and engineers. (One project representative observed that the project has taken only four years because funds are derived from legislation pertaining to veterans, not general fund outlays, resulting in fewer legally mandated budget reviews.)

The building is a six story structure with 110,000 net square feet. The project "includes renovation of the existing tenant improvements on the first, second, third and sixth floors and public spaces on the fourth and fifth. Demolition includes removal of asbestos throughout the building and removal of an obsolete cooling tower on the roof. Improvements include a new roof and handicap [accessibility] upgrades. Renovated areas equal 85,000 square feet." (Source: OPDM Capital Outlay Cost Estimate, March, 1990)

The total construction cost for the work is estimated at \$5.02 million. The total project cost is \$7.38 million, including a substantial amount for modular office systems. Asbestos removal is estimated at \$310,000.

On a first cost basis (considering only construction cost) the construction of a replacement facility elsewhere in Sacramento appears to be substantially more than the planned renovation. At \$115 per square foot, a new office building of about 120,000 gross square feet would have a construction cost of nearly \$14 million, exclusive of land costs, parking, and project costs (\$115 /square foot x 120,000 GSF). The square foot cost

of \$115 is based upon \$75/sf for structure, shell and core and \$40/sf for tenant improvements. These figures are based upon discussions with Hanscomb Associates' cost consultants about recent projects in the area and the level of quality expected in a state office structure. This figure is comparable to current square foot figures used in the OPDM cost model.

If a project to construction cost ratio of 1:1.15 is used, the total project cost for a replacement facility would be about \$16 million. However, the scope of work for these projects is not completely comparable since the renovation does not involve significant work to the fourth and fifth floors, and other work on this older building may be necessary in the future.

Conceptually, leasing an equivalent office space also appears to be a far more expensive alternative to remodelling in the case of Veteran's Affairs. A 110,000 net square foot area would generate a gross rent of \$1,430,000 per year at a rate of \$1.11/sf/month which is the current average lease cost for state occupied space. Thus the gross rent for a leased project would be equivalent to the construction cost for the Veteran's Affairs remodel after only three years, and would match or exceed the project cost after four and one half years.

PARTIAL FUNDING OF SPECIAL BUILDING REPAIRS

The DGS Office of Buildings and Grounds prepares an annual request for a five year funding for special building repairs which are classified into six priorities. The priorities, as outlined in the Eighth Supplement, are:

- Priority 1: Health & welfare of building occupants
- Priority 2: Compliance with fire and life safety, seismic safety, and handicapped accessibility codes
- Priority 3: Building Security
- Priority 4: Efficient operation of building systems
- Priority 5: Building environment conducive to comfort & productivity of employees.
- Priority 6: Visual aesthetics & preservation of state property

As DGS' most recent Five Year Plan for Special Repairs notes, "First priority projects are those necessary to prevent harm to the building's users or to avoid damage to state property." However, even these first priority projects are not always funded in a timely manner. For example, the Office of Buildings & Grounds submitted a request for a new roof for the Resources Building, a seventeen-story structure with over 550,000 square feet of space, for five consecutive years before funding was approved.

Lack of funding for "Special Repairs" budget requests limits DGS' abilities to meet its mandate to "protect the health and welfare of building occupants and to preserve the state's investment in buildings and grounds."

POTENTIAL ADDITIONAL COST OF ASBESTOS ABATEMENT

Asbestos abatement is still the topic of an intense national debate, and there are significant disputes on the extent of the health hazard to building occupants exposed to different types of asbestos. Some sources estimate the total national cost to remove all asbestos from older buildings at over \$100 billion. In some instances, replacement of older buildings may be preferable to extensive asbestos abatement, particularly if the building is small, old and has other rehabilitation needs.

In 1986, OSA conducted an extensive survey of the presence of asbestos in 12,000 state-owned buildings. In the survey, buildings were classified into three priorities depending on level of health risk based on a model developed by the Environmental Protection Agency.

Priority One included high-risk facilities where abatement should be carried out immediately. Priority Two facilities required abatement in the "short term" and Priority Three projects were considered low risk. The OSA study was a "passive" survey. While identifying exposed asbestos, no destructive testing was done.

The data from the OSA survey is a valuable element in assessing the feasibility of restoring older state buildings,. However, asbestos data must be considered in concert with other information on building condition and functional needs. Without detailed data for each building, determining whether replacing a building is more cost-effective than performing extensive abatement is not possible.

Significant abatement projects have been undertaken at 1120 N Street (the CalTrans Building) and the Resources Building at 1416-9th Street. Costs for abatement can vary significantly (\$3-30/sf); the current project for the Veteran's Affairs building at 1227 O Street includes the removal of asbestos from the entire facility which is estimated at \$310,000 or \$3 -\$4 per square foot for the entire structure.

Another component of the asbestos abatement program involves asbestos removal as part of tenant agency office modernization programs, regardless of the nature of the hazard. An example is an office modernization project for the Water Resources Agency, the principal tenant of the Resources Building at 1416-9th Street. Two floors were

remodeled to provide modern open office environments. The total cost of the two projects was over \$280,000, including asbestos abatement.

Additionally, OSA staff have noted that the presence of asbestos in leased office space has not been ascertained (the state asbestos survey did not include the older leased office buildings). Currently, building owners are required to certify that facilities they lease to the state are free from the hazards of asbestos. However, in a recent case, a fire in a state-leased building in Los Angeles resulted in the discovery of asbestos despite the owner's certification. The lack of definitive, verifiable data on the presence of asbestos in office buildings leased by the state suggests the need to develop mechanisms to sample the leased office stock for asbestos, and also for other infrastructure conditions such as seismic stability.

ADDITIONAL RESTRICTIONS FOR HISTORICAL BUILDINGS

Eight of the twenty-two buildings in the capitol area are fifty years or older. The oldest structures comprise only 28% of the stock, including three structures listed on the National Historic Register: Unruh, Supreme Court & Library and the Blue Anchor Buildings. Two of the remaining five will be demolished for the Site 7 State Archives project. The three remaining buildings (Consumer Affairs, Caltrans, Food & Agriculture), which have a total of about 640,000 NSF were constructed in 1936-37.

Historic preservation regulations apply only to a small number of the state's older office buildings in Sacramento. The three buildings currently on the National Register not only have symbolic value, but also enjoy strong constituent support; it is fair to say they will continue to be maintained as state office buildings. The three contiguous office structures on N Street represent the remaining buildings which are potentially affected by preservation concerns. Restoration and modernization of the remaining seventeen buildings is not adversely affected by historic preservation concerns.

RECOMMENDATIONS

The state should prepare detailed, systematic assessments of all older state-owned office building stock in Sacramento. A model for these assessments would be the OSA infrastructure studies of the state's San Francisco Bay area office facilities and aggregation of data from existing studies. The principal elements of typical infrastructure studies are outlined below.

Fire and Life Safety

Maintaining the health and safety of state building occupants and protecting the state's property are two central DGS objectives. Fire & life safety studies are necessary to document existing conditions for comparison with codes. Typically these studies include a careful review of exiting, fire detection, alarm and suppression systems, fireproofing, and materials.

Structural/Seismic Safety

Seismic safety has become a high priority for structures in the coastal regions since the October, 1989 Loma Prieta earthquake, but it is also an important consideration in assessing long-term use in office buildings in Sacramento. The governor's recent executive order and the passage of Proposition 122 affirm the importance of seismic evaluations in state facilities.

Structural framing systems must also be evaluated for their potential to accept different uses with heavier loading and to permit implementation of open office schemes.

Asbestos Study

Though an asbestos survey has been completed on these facilities, it is often necessary to complete more detailed analysis in developing the optimal, long-term abatement strategy. (More detailed destructive testing will continue to be necessary before remodeling can occur on "suspect" buildings.)

Building Systems and Energy Conservation

Assessments of plumbing, electrical, mechanical system condition, efficiency, and retrofit potential are critical to a comprehensive study of a building's physical life since they represent a substantial element of both construction and life cycle costs.

Handicapped Accessibility

Handicapped accessibility has been provided in many of the state's older office buildings according to the CAP Progress Report of 1983. However, documentation of improvements and identification of additional needs should be part of all building assessments.

Environmental Conditions

Employee productivity, retention, and absenteeism can be affected by the quality of the work environment. Modern office designs include provision for daylighting and glare control, efficient, energy-conscious artificial lighting, and acoustical control. Existing office environments must be evaluated on the basis of current standards and the potential to modernize or upgrade those spaces.

Functional Conditions

Functional obsolescence has rendered many older buildings obsolete although their structure and mechanical systems are sound. Open office design and increasing use of personal computers have changed the way office spaces are organized. Some buildings readily permit extensive modification, while others are limited by the presence of numerous load-bearing walls. A related concern is the ability of an office floor to accept

computer raceways and additions or changes to lighting, electrical, and mechanical systems. These conditions are even a problem in newer state buildings such as 4949 Broadway where there is an increasing need to add computer capacity to this seven-year-old facility.

Increases in the size and organizational complexity of a government agency has created a demand for larger floor plate areas to assure reasonable staff efficiency. In the case of Sacramento's older state office facilities, there may be a mismatch between floor plate size and the operational efficiency of tenant agencies, particularly in the smaller buildings. Smaller buildings may also limit the potential for agency consolidation. For example, the original tenant agency (Education) of 721 Capitol Mall has grown significantly since occupying the building in the mid 1950's. Identification of any mismatch between facilities and long-term needs of current tenants is an important part of a functional analysis.

Historic Preservation

Concern for historic preservation is a legally mandated requirement in planning for buildings which are least 50 years old. Preservation studies will be important in five or six of the older buildings. The three buildings listed on the National Register have been studied extensively (Unruh, Supreme Court and Library, and the Blue Anchor Building). Priority should be given to assessing the historic potential of the N Street buildings (Consumer Affairs, CalTrans and Food and Agriculture).

Rehabilitation Costs/Levels and Phasing

Conceptually, each restoration project could be modelled to have several levels of restoration based upon need, condition, and available funding. Priorities could be assigned according to the Office of Buildings & Grounds system or a similar system, which ranges from health & safety concerns to exterior aesthetics.

Each assessment should include comparative economic analysis of renovation and new construction based upon the OPDM Economic Forecasting Model.

Expansion Potential / Site Potential

Many architectural programming studies lack an adequate emphasis on the need to accommodate change and expansion. For existing buildings it is important to assess the nature and extent of potential expansion. Related considerations are site coverage and land-use intensity. Studies of land-use intensity are used to determine if expansion or replacement with new buildings would yield a more efficient and economically beneficial use of the land.

Interim Housing

Each study should address options, costs and benefits of housing tenant agencies during the renovation period. Outlining these options early in the process will make overall planning more rational.

Priorities

A brief conceptual study of the planning for the state's older office facilities cannot pretend to identify all of the priorities in terms of upgrading the existing stock. However, several priorities have emerged as logical points of focus.

In terms of seismic safety, priority should be given to a detailed analysis of the high-rise buildings: the Resources Building at 1416-9th Street and the Health Services Buildings at 714 -744 P Street, since taller buildings may be affected by long wave shock from coastal earthquakes.

Another priority should be detailed studies of the Consumer Affairs, the Caltrans, and the Food & Agriculture buildings along N Street, since these facilities are quite large and are potentially eligible for the National Historic Register.

The state should formulate an existing facilities master plan element to establish priorities and phasing for a restoration/modernization program. This element flows from the detailed infrastructure studies outlined above and is integrated with the office element of the CAP.

The state should streamline the process for planning and budgeting for all major projects. If state capital outlay funding is not available, the state should explore other means to finance rehabilitation through sale leaseback to private developers or public agencies, as outlined in the Eighth Supplement.

As part of the master plan process, the state should study selected privately-owned office space in or near the core area to determine the economic feasibility for purchasing existing buildings for conversion to state office uses. In order to meet the need for increased office space the state should study the feasibility of buying selected office buildings in the central city. In some cases, if infrastructure studies show that state requirements are met, then it may be cheaper and faster to purchase existing privately-owned office buildings.

Chapter 8

Recommendations

CHAPTER 8 RECOMMENDATIONS

This chapter presents Consultants' recommendations for improving implementation of the Sacramento Facilities Plan. Consultants believe the Sacramento Facilities Plan is fundamentally sound and that, with a few specific exceptions discussed below, implementation of the policies set forth in the plan will provide maximum public benefit to the citizens of the state. In the following discussion, Consultants present a number of improvements that can be made in the planning process itself. However, none of the specific problems that these recommendations address will automatically result in plan implementation.

The reasons the plan has not been implemented are discussed in detail in this report. However, before starting on specific recommendations, Consultants summarize the basic causes of lack of implementation.

- No one is exercising the leadership necessary to implement the plan.
- The existing planning structure is complex, with fragmented responsibilities and limited authority given to the various actors.
- Some of the assumptions and conditions in the plan are no longer valid, and no attempt is being made to meet the goals associated with them.
- Capital outlay funds are no longer available.
- Despite the lack of capital outlay funds, the state is not making good use of alternative financing methods.
- The funding process is lengthy and uncertain.
- Contrasted to the capital outlay funding process, the alternative of leasing is much easier and faster.

Consultants stress that the basic recommendation addresses the lack of leadership.

The state of California, including the new administration and the legislature, must decide if it still wishes to implement the Capitol Area Plan and the Sacramento Facilities Plan. If it does (or has only minor modifications), a clear commitment to do so is required.

The following recommendations, which should be viewed in light of the reasons for the failure to date, address both specific procedures and general issues. These include the state's planning structure, the original plans, financing methods, and planning policies and processes. Full discussion of the issues supporting each of the recommendations is presented throughout the report.

PLANNING STRUCTURE

The state should examine and revise the existing planning structure to enable better implementation of the policies.

- The state should establish a high-level policy-making body, composed of representatives of both the Executive and Legislative Branches, to set development priorities for the planning office, and to decide among the proposed alternatives. Consultants do not specify the composition or structure of this body except to say that its membership must be at a level where it will clearly have the authority to implement its decisions.
- The planning functions directed towards construction, rehabilitation, or leasing - now divided among OPDM, OREDS, and OSA - should be reorganized to eliminate current confusion and inefficiencies. This office should utilize a comprehensive computerized data base for planning and tracking progress of both the overall plan and individual components.
- This office should have substantial input into, and oversight of, planning of all facilities in the Sacramento area, including projects being developed by the legislature and departments now exempt from DGS control.

REVIEW OF PLAN ASSUMPTIONS

The Sacramento Facilities Plan and the Capitol Area Plan should be reviewed and the goals modified when warranted by changing conditions or flawed assumptions. With the exception of these modifications, the original goals of the plans should be maintained and supported. Specific areas that should be reviewed are listed below.

- Development north of L Street should no longer be a goal.
- It is not necessary to adhere rigidly to the quarter-block development concept, particularly for parking structures. The spirit of the plan can be maintained by promoting mixed-use development on adjacent blocks.
- The goal of reducing the proportion of single-occupant vehicles to five percent by 2000 is unattainable; this figure should be raised to a realistic level.
- The reduction of leased space remains highly desirable, but leasing should be used for short-term needs and whenever else it is truly advantageous. The fraction of leased space will change with conditions and should not be forced into an arbitrary fixed value of ten percent, which is probably unrealistic.

FINANCING METHODS

The state should seek long- rather than short-term economic benefits in space acquisition. Even though capital outlay would be the cheapest way to build, the funds are not available. Alternative financing, generally by lease-revenue bonds, should be the first choice in most development proposals.

- The state should continue to actively review and evaluate alternative financing routes.
- The state should explore the feasibility of purchasing existing buildings, especially those it presently occupies.

Straight Leasing vs. Lease Purchase (Bond Financing)

- The state should own the buildings required for office space rather than use a straight lease to accommodate this need. Ownership applies to existing and future buildings. Tax-exempt bonds and/or notes should be used to buy existing buildings or raise money for new buildings.
- Whenever the state negotiates a straight lease, it should always negotiate an option to purchase the building.
- In most circumstances, the state should not use private installment sale financing to take ownership of a building at the end of the rental payment period unless it is not able to finance ownership with tax-exempt bonds.

The Master Space Planning Process

- The State Treasurer's office should provide DGS with an annual amount of bonding (lease revenue bonds and/or certificates of participation) that it believes the state's general fund can support for the department's Five Year Capital Planning Process.
- The Master Space Planning Process would establish policies and criteria to allocate the available annual bond volume between new office construction for DGS' Five Year Capital Plan and the purchase of existing buildings.

Financing Techniques and the Economic Forecasting Model

- The state should include asset substitution and short-term note financing alternatives in the Economic Forecasting Model (EFM).
- When selecting an "average coupon yield," the state should determine whether the rate used already incorporates the underwriter discount fee and other costs of issuance.

- If the proceeds of a bond issue (except the debt service reserve fund) can be spent in two years according to the following schedule:
 - 10 percent spent within 6 months
 - 45 percent spent within 12 months
 - 75 percent spent within 18 months
 - 100 percent spent within 24 months

the state should use the earning's rate from the Pooled Money Investment Board as the earning's rate in the EFM bond's construction and capitalized interest fund. If the construction period is greater than two years, then the state should use the arbitrage yield of the bonds as the earnings rate for the construction, capitalized interest and debt service reserve funds.

- For each asset in the Proactive Asset Management data base, the state should indicate whether it is available to use as collateral in a lease revenue bond financing.
- When planning a bond issue for office construction, the state should identify assets in the Proactive Asset Management data base that can be leased as a substitute for the lease on the proposed new building. The state should use the asset as a substitute whenever possible to eliminate capitalized interest expenses.
- When planning a bond issue, the state should evaluate the use of short-term tax-exempt financing during the construction period.
- The effect on the tax-exempt status of bonds issued for a state-owned building that has space for "non-public" purposes, such as cafeterias, concessions, and child care, needs to be further explored.

THE CAPITAL OUTLAY FUNDING PROCESS

Unless capital outlay funds once again become plentiful, they should be used only for the preconstruction stages of a project and for major repairs. Construction of a building should not be dependent on the availability of capital outlay funds.

- The funding process should be streamlined, when possible, to reduce substantially the time required to construct new facilities.
- After a building project is initially approved, it should not be subject to cancellation or long delays, except in the most extreme and unusual circumstances.
- The state should consider establishing an independent authority (or empowering CADA) to develop projects free from annual political review once those projects are approved by the governor and the legislature.

PLANNING POLICIES AND PROCESS

- Updating and maintenance of the CAP and the Sacramento Facilities Plan should include more detailed annual agency surveys. Employee transportation patterns should be sampled every two years.
- The location and consolidation study addressed in the Sacramento Facilities Plan should be updated. It should provide a systematic and rational guide to locating agencies in the core area. This analysis should be made part of the state's ongoing planning activities.
- The consolidation and locational criteria should include multidepartmental consolidation and should recognize proximity to the capitol as a scarce resource.
- A detailed systematic assessment of the condition and rehabilitation status of all older buildings in Sacramento should be made.
- The Statewide Property Inventory should be the data base supporting the planning. The planning office may find it necessary to augment data from the SPI with information of its own, but it should not set up a separate and perhaps inconsistent data base.
- A leasing policy consistent with the consolidation and location goals of the CAP should be developed and instituted.
- The state should evaluate the success of the specially-designed and experimental buildings constructed in the early 1980s and incorporate the results into the plans for future facilities.
- Other factors in addition to department heads' predictions should be used to forecast staffing and space needs. Overall Sacramento area staffing as well as individual agency requirements should be examined.
- The sizes of core area and peripheral parking facilities should be reexamined in light of the revised transportation mode split goals.
- If peripheral parking is to be retained, incentives such as subsidizing the parking fees and shortening the shuttle bus transit times will need to be developed.
- Provision for telecommuting and child care should be explicitly included in the revised plans.
- The planning office should prepare an introductory guide to the planning and financing process for use by department administrators, legislative staff, and other involved parties. It should also maintain a concise history of the progress of projects under its jurisdiction.

Appendices

APPENDIX A

SUMMARY OF SURVEY ON OTHER STATES' FACILITIES PLANNING APPROACHES

As part of assessing the goals, objectives and policies for the planning and financing of new and remodelled office space for California state agencies, Consultants conducted a survey of progressive states for comparison.

Eleven states and the Province of British Columbia were contacted, specifically, the agency responsible for planning and financing office space. The states surveyed were Delaware, Hawaii, Illinois, Louisiana, Maryland, Michigan, Minnesota, Missouri, New York, Ohio and Washington.

The survey revealed that few states had comprehensive facilities master plans in place. A few states were in the process of developing such a plan (Delaware, Louisiana, Missouri). The states which did not have master plans indicated that their systems were driven by the political arena. For these states, the allocation of funds to projects was dependent in large part upon the willingness of the legislature to respond to a particular agency. The fiscal year cycle, with yearly appropriations, required some states surveyed to undergo a new request process every year (like California's process).

States which appear to have comprehensive facilities master plans in place include New York, Maryland, Illinois and Washington, and the province of British Columbia. New York has a centralized process that is highly administrative rather than legislative. This enables the state's Bureau of Space Planning and Allocation to submit assessments systematically, with future needs projected.

Of states with master plans, the most unique was the province of British Columbia which in 1978, established the Building Corporation, a private corporation, to handle all of the planning, building and leasing for governmental agencies. The corporation is autonomous and free to determine its policies and make decisions independent of the legislature. With this system, the province can establish comprehensive and far-sighted plans.

Most of the surveyed states had several projects in the planning or construction phase. The length of time to complete these projects ranged from two years to seven years, from initial planning to occupation. The state with the least amount of leased space at nine percent was Maryland. Michigan had the largest amount at 70 percent in the capitol area.

The policy towards leasing for most states is to avoid it if possible. Several states have determined that leasing costs over an agency's length of occupation are greater than construction of new, state-owned space. The benefit of leasing some space is that it allows flexibility to either expand or shrink with agency size fluctuations. British Columbia, Delaware, Illinois, Louisiana, Maryland, Michigan, Minnesota, Ohio and Washington are all attempting to decrease the amount of leased space either by consolidating agencies, or by purchasing currently leased space.

Hawaii is in a unique position as the government is in the planning phase of a satellite city development on the opposite side of the island in order to reduce congestion in Honolulu. Until the satellite city is developed, the state must lease space. Once the new area is in operation, it will include a Telecommunication Conference Center for video communication.

Although states are attempting to decrease the amount of leased space, most have experienced an increase. The increase is due to greater demands for space and the comparative ease of acquiring leased space to meet short-term needs (as opposed to construction or other means of acquiring state-owned space). Only two states surveyed, Delaware and Michigan, have experienced a decline in the amount of leased space. This decline was the direct result of aggressive policies towards acquisition and consolidation.

Almost all of the states use bond financing to fund new office construction and remodelling. The only exceptions were Washington, Maryland and New York, which have developed various techniques to meet the concerns of their particular environment. Few states have used any lease purchase agreements to fund their projects. Those who have done so in the past are Delaware, Louisiana, Michigan, Missouri and New York. All of these states have used lease purchase arrangements for less than ten percent of their total projects. However, most states expressed an interest in using lease purchase, or increasing its usage, as an option .

Half of the states surveyed had a needs assessment to upgrade older office buildings. Some of the needs assessments are incorporated into the state's facilities master plan; some were in a separate document. For British Columbia, the needs assessment provides projections for the province for the next ten years. For the states that do not have a data base or inventory of facilities, there was generally an informal mechanism for assessing needs.

Eight of the twelve states surveyed had a stated asbestos abatement policy. Those without a formal policy indicated that abatement would occur if there was a clear danger, such as when a building was remodelled (except Louisiana which was requesting proposals to further determine which state-occupied buildings contain asbestos). All states except Louisiana have conducted an asbestos survey for older state office buildings.

A table summarizes the findings of this survey. It is followed by survey findings for each state contacted.

Survey of Facilities Planning in Other States

State	MP	Out-line	Length (yrs)	% owned / % lsd	Lease Amt (increasing/decreasing)	Funding	NA	Abatement Policy		
B.C.	YES	NO	3	75 / 25	INCREASING	BOND	YES	YES		
DE	NO	NO	2	NA	DECREASING	BOND	NO	YES		
HI	NO	NO	5	75 / 25	INCREASING	BOND	NO	YES		
IL	YES	YES	2.5	65 / 35	INCREASING*	BOND	YES	NO		
LA	NO*	NO	3	68 / 32	DECREASING	BOND	YES	NO*		
MD	YES	NO	2.5-10	91 / 9	SAME	*	NO	NO*		
MO	NO	NO	2.5-3.5	30 / 70	DECREASING	BOND	NO	NO		
MN	NO*	NO	6	43 / 57	INCREASING	BOND	NO	YES		
MS	NO*	YES	3	60 / 40	INCREASING		NO	YES		
NY	YES	YES	31446	48 / 52	INCREASING	VARIES*	YES	YES		
OH	NO*	NO	2 to 4	NA	INCREASING	BOND	YES	YES		
WA	YES	NO	4 to 7	50 / 50	*	VARIES*	YES	YES		
* indicates the reader should refer to the summary										
All numbers and percentages are estimated. For further information, refer to summary										
For key to column headings, see Survey Questionnaire.										

British Columbia

British Columbia (B.C.) has a private corporation, the Building Corporation, which is responsible for handling all the planning, building and leasing for governmental agencies. It is a "crown corporation" because the main shareholder is the government. However, the corporation is free to control its operations and is an independent entity that makes its own decisions. The Building Corporation was established in 1978, and was preferred over a governmental ministry primarily because the existing ministry was inefficient and the province was in a financially tight situation. It was felt that a corporation could more easily control its internal process as well as obtain a good quality costing of programs and agencies. Additionally, the staff of the existing corporation is less than half of the staffing under the ministry.

B.C. has a comprehensive needs assessment which is a "driving force" in their operations. All information is computerized in a data base, and the province has projections for the next five years. It has computerized the spaces of all of the governmental agencies (over 20 million sq. ft.). The system is comprehensive with a master plan for key cities that is updated often. In Victoria, where available space is tight and careful and timely planning is required, the master plan is updated every six months. In Vancouver, where there is an active lease market, it is updated every two years. The plan does not include all three functions (legislative, judicial, executive), since the corporation charges individual ministries (their "clients") for the cost and the clients in turn request funding from the legislature.

B.C. does not have a written outline of the process used to plan and build new space, as it generally doesn't construct buildings unless they are needed for a special purpose. The corporation leases space more often than it purchases space. It has a complex process that goes through the Board of Directors, Treasury, and "casually" through the government for approval before building. Every project varies as does the process for each.

The corporation is in the process of leasing 80,000 sq. ft. of office space, which led to the need for construction of a new building. A 130,000 sq. ft. building is to be constructed, and the province plans to lease for a ten-year period. Another 130,000 sq. ft. building is being constructed by the corporation itself in Victoria. The Corporation is building rather than leasing in this case because the agency that will occupy the space has special requirements and it is projected that it will occupy the facility for several years.

The length of time from initial planning to occupancy varies. If the corporation constructs a building on its own, in which case the requesting agency goes to the legislature for funding, three years can elapse for new construction. The leasing process is less time-consuming. If there is a renovation, the time to complete a project increases. B.C. tries to spend as little money as possible until the "go" phase.

Of all governmental office space, 25 percent is leased. In Victoria, the aim is to own 70 percent of the space, but the reality is 60-65 percent owned. In Vancouver, it doesn't matter how much space is leased; the percentage can be high, unless the cost is high, in which case the province attempts to own. The province's average goal is a 50-50 or 60-40 split. At this writing, the leasing of space had been increasing in the province.

During the 1980s, the corporation was increasing the amount of leased space. It is now pulling back from this policy and considering the "residual value." However, in spite of this, it is finding that the long-term costs of leasing are higher than other options. B.C. has found that with a lease proposal in Vancouver it can get competitive bids. The bidders

acquire low-rate financing from mortgage banks which see little risk in an operation guaranteed by the government.

The Corporation borrows funds to finance projects. The agency requesting the space goes to the legislature and asks for an approval of the rent as determined by the Corporation. The Ministry of Finance is responsible for all funding at a preferential rate; it requests funding from the legislature. The financing is the equivalent of bond financing. It is a lump sum allocation, however; that is, individual projects are not individually funded. Instead, a lump sum is earmarked for construction, and the number of facilities or projects. They do not use lease purchase, although it has been discussed as an option.

The corporation has a very aggressive asbestos abatement policy and has control programs. All buildings have been surveyed.

State of Delaware

The state of Delaware does not have a comprehensive master plan although it is developing one for the Wilmington area. Planning is done on a case by case basis, and no standard process is used to plan new space. Delaware consists of three counties; most state functions occur in two of these. A space planning study is being conducted by a private court specialist and an architectural planning firm for the City of Wilmington. It will include the court fields and legislative functions and long-range staffing projections, and will request funding for the next phase. Currently, the master plan is in the final draft stage.

The next phase will suggest some creative financing options because the state does not want to use bond financing. In Dover, the state capitol, the state is in the process of consolidating the leased facilities into one state-owned facility. The total amount of square footage is between 60,000 and 70,000 sq. ft.

The consolidation of leased facilities totaling 60,000 to 70,000 sq. ft. into state-owned land in Dover will be financed by a bond bill of approximately \$6 to \$7 million. This consolidation will house the administrative and some legislative functions, and those agencies that have few clients. The debt service for this project must have negative or equal impact to the current leasing policy. In fiscal years 1989-1990, the state undertook the first real estate acquisition program. Statewide, five major buildings which were formerly leased are being acquisitioned into state-owned space. Funding was provided by a Certificate of Participation. The acquisition program represented a net savings of \$5 million dollars to the state.

It takes approximately 18 months to 2 years to build new state office space for projects under 100,000 sq. ft.

The state leases 450,000 sq. ft. statewide, 30 percent less than before the recent consolidation. Since each department maintains its own inventory, there is no known total amount of state-owned space. The state is actively decreasing the amount of leased space currently.

Lease purchase is used for less than ten percent of construction projects. The majority of projects are funded by bond financing.

While the state does not have a needs assessment, it does have a deferred maintenance program.

The state has surveyed state-owned buildings for asbestos.

State of Hawaii

Hawaii does not have a facilities master plan, but it is proposing the institution of computer-aided design (CAD) of space so that data can be computerized. When CAD is put into operation, it will include all functions (legislative, judicial, and executive) and will be updated as information is added. The state does have an inventory of leased space with the newly created leasing branch.

An agency requesting space must complete a Space Needs Computation Form which lists all the agency's requirements. This form is currently being reworked since it is not a comprehensive listing. No written outline of the planning and construction process exists. In the capitol area the state is moving towards short-term, lease-based occupation until Kapolei (described below) is built up.

Current projects include construction of a new facility for the Archives Department. The project includes a site selection study, budget, etc. Also, because the capitol building needs abatement and renovation, a new state office tower is being built. The legislature will occupy the building for three years while the capitol work is done.

Generally, the process from initial planning to occupancy of state-built space takes approximately five years. Each phase must be approved by the legislature (i.e., planning, design, acquisition and construction). If necessary, funds from one phase of the project may be requested for completion of another phase.

Currently, 1.2 million net sq. ft. is owned and approximately 300,000 is leased. The state has increased the amount of leased space, but only in response to short-term need and because it does not want to construct any new buildings in the capitol area. The state is building a "second city" called Kapolei. Part of the plan for the city requires that construction of all new buildings begin within the next ten years. The plan is an effort to cut down on the traffic in Honolulu and will include a "telecommunication conference center" where state agencies on opposite sides of the island, and on different islands, can communicate with each other via live video. All buildings in the city will be state-owned.

To finance construction of office buildings, the state uses both the general fund and bond financing. The state does not compile data regarding how much each of these methods is used; however, staff noted that lease purchase is rarely used.

Hawaii does not have a current needs assessment. A series of studies have been conducted and approximately every two years the state will "go in and know the basic game plan." There is a project development report, and while it is being completed, funds from the legislature are being requested.

The state has an asbestos abatement policy to remove asbestos whenever a remodel occurs. Part of the reason that the capitol is being renovated is to remove asbestos. The state has done a survey of the state buildings.

State of Illinois

Illinois has a comprehensive facilities master plan that includes all three branches (legislative, judicial, and executive). It was modified and adopted in 1975. In 1988, the governor set up a panel to review the document, and since then it has been updated by the Government Council of Planning twice per year.

A written outline of the process used to plan and build new state office space is included in the master plan. A commission looks at current and future need, growth patterns, testimony from different groups, etc. to determine its decisions.

There are several examples of recent projects. The total master plan calls for \$150 million over the next seven years.

1. Tourist Center - completed in 1989. \$3.5 million with a 9,000 sq. ft. building, 5,000 sq. ft. auditorium, a picnic area, parking for 50 buses and hundreds of cars, etc.
2. State Library - \$40 million with approximately 100,000 sq. ft.
3. State Armory - rehabilitation of entire armory of 150,000 sq. ft.
4. State Police - planning for new headquarters. Approximately \$35 million with 150,000 sq. ft.
5. Appellate Courts - 15,000 - 20,000 sq. ft. in the planning stage.
6. Day Care Center - for state employees; in the planning stage.
7. Parking Structures - two 700 car structures; in the planning stage.
8. Landscape Plan - working in conjunction with the City of Springfield to devise a comprehensive plan for the entire capitol area.
9. Museum Addition - approximately 200,000 sq. ft.

The length of time from initial planning to occupancy is approximately 2.5 years.

In the capitol area, approximately 65 percent of office space is owned and 35 percent is leased. Farther out in the city, leased space increases. While the state recognizes the need to have some leased space due to the fluctuating space needs of state agencies, it is trying to convince the legislature to steer away from it. In the past five to eight years the amount of leasing has increased. This was due to economic recession nine to ten years ago; budgets were very tight, interest rates were high and it was easier to appropriate small amounts towards yearly leases than large sums for purchase. Now, the state is attempting to decrease the amount of leased space through the option to purchase and other methods.

Practically all construction of state buildings is bond-financed. Any major building that is leased has a purchase option (usually after five years), but the state does not always utilize it. The type of financing varies from building to building.

The state has a data base, and it is currently in the process of reviewing it. It also has a fairly comprehensive needs assessment.

As long as there is no immediate danger, asbestos abatement is not done. If a building is being remodelled, or it is found that the asbestos is not encapsulated, then abatement occurs. All buildings have been surveyed and Illinois is currently reviewing a seven-volume report.

State of Louisiana

Louisiana has contracted to have a comprehensive master plan prepared that will be completed in six months. It will cover all three branches of government except some exempt legislative functions.

It does not have a written outline of the process used to plan and build new state office space. All requests go through a capital request process:

1. Agency submits request with specifications to Facility Planning.
2. Facility Planning reviews it and submits it to the legislature.
3. Legislature then approves.

There are several examples of current projects. The state is currently acquiring state-leased buildings. It is trying to purchase buildings using a corporation that is a non-state entity. It has an agreement with this leasing corporation and will finance through bond sale.

For a typical (over 100,000 sq. ft.) administration building, the acquisition process takes approximately three years.

In the capitol area, approximately 600,000 to 700,000 sq. ft. is leased and 1.5 million is owned. Statewide, the total leased space is approximately 1.8 million and 2 million sq. ft. owned.

The state is decreasing the amount of leased space through the consolidation of agencies and through acquisition of currently leased space.

Funding of new and remodelled state office space is primarily through bond financing. Lease purchase is rarely used.

Louisiana has a statewide inventory, but it isn't complete. Upgrades are conducted on a case by case basis.

The state has an RFP out to determine which state-occupied buildings that have asbestos. Once this is complete, it will conduct abatement.

State of Maryland

A master plan was developed in 1967 for the Annapolis area. The plan has been updated twice, and 17 out of the 20 master plan recommendations have been implemented. There is no written outline of the process used to plan and build new state office space. Each department submits its needs to the Office of Planning where it is reviewed and submitted to the governor, and then to the General Assembly. A comprehensive program manual is used to assess needs, which includes justifications for space requirements.

Currently the state is constructing a 122,000 sq. ft. building in the capitol area, at a cost of about \$15 million, to house the Department of Housing and Community Development and the Department of Environmental Services. There are no other current projects because state office buildings are rarely approved. The priority is to build prisons and universities.

Maryland maintains 51,654,290 sq. ft. in office and storage space. Of this, approximately 47,000,000 sq. ft. is state-owned. The remaining amount, 4,654,290 net square feet, is leased at an annual cost of about \$45,000,000. The above figures account for all state offices and institutions, including prison facilities, hospitals, and state colleges and universities.

The general policy concerning leasing is to lease only when necessary. When the state finds that it is leasing a great deal of office space, it will attempt to either purchase or construct a building to house agencies currently in leased space. The state is attempting to increase owned space, and consequently decrease the need for leased space, through the "District Court Multi-Service Center Building Program." Fifteen agencies have been consolidated according to this program at a cost of \$70 million.

For funding, the state uses general obligation bonds which are a state commitment and are backed by state property tax revenue. Last year, \$330 million was allotted as the new issuance of debt, and this covered all state construction costs (including costs for prisons).

An agency called the Capital Debt Affordability Commission determines how much debt can be authorized each year in accordance with sound financial practices. They are required to review the size and condition of state debt on a continuing basis and the needs previously identified by the Department of Budget and Fiscal Planning, as well as a variety of factors related to the ability of the state to meet its projected debt service requirements and marketability of state bonds.

The state is anticipating new asbestos abatement laws. Currently it has a unit that does large scale removal. The limit is 160 linear feet per project, or 260 linear feet per year. Every state building has been surveyed.

Three documents of special interest are: 1) The Maryland State Capital Budget Formulation Process, a paper describing the capital budgeting process; 2) Instructions for the Preparation and Submission of Capital Project Reports for State-Owned Facilities, which provides detailed instructions for use by state agencies and departments in preparing their annual capital budget requests; 3) "Capital Improvements Authorized by the General Assembly, 1975 through 1989," a publication updated annually that provides a running fifteen year history of the state's capital budget.

State of Michigan

Michigan does not have a comprehensive long-term plan because it can never get a plan accepted by every state interest. The state must work within the directive of a past governor to centralize space within the capitol area. To abide by the directive, the state is obtaining vacant lots within Lansing. The directive was the result of a plan to create "satellite" state agencies outside of Lansing. Several groups protested, and the governor responded by directing state agencies to centralize within Lansing.

The state does not have a written process for planning and building new state office space. Every year it assesses the needs of the agencies requesting space, then it processes these needs through the Department of the Budget which determines what the state can afford. Once this determination is made, a proposal is submitted to the governor and the legislature. Since every year is different and is dependent upon the funds available, lobby activity, etc., the state does not know how much will be allotted or to which agency. The state has a "Capital Outlay Manual" which outlines some of the allocation processes.

There are several examples of current projects using this process:

1. All universities.
2. Library/Historical Center built in Lansing Capitol Complex area which is a "showpiece" building that is approximately 300,00 sq. ft. and costs \$42 million.
3. Olds Hotel - a project to renovate an historical hotel with ties to Oldsmobile. It is being purchased by the state and converted into office space. The total project cost will be \$25 million (\$3.4 million for the building purchase) and will be approximately 250,000 sq. ft.

For the library, the process from the time of approval to occupancy was approximately 28 months. For the Olds Hotel (not yet completed), approximately 18 months from the time of approval to occupancy will be required. The time frame for initial approval: requests are made in November and are finalized in February by the Department of the Budget, then the Legislature sees them and final approval is given by October.

In the capitol area, approximately 30 percent of state office space is owned. When an agency requests space, the state attempts to first place the agency in state-owned space. If it cannot obtain owned space, it leases space. A separate division performs the leasing function. The state tries to construct buildings without using developers. When the leases a space, it generally is responsible for the maintenance; this is another reason that the state generally avoids leasing. The amount of leased space has declined due to efforts to decrease space needs in the capitol area.

Almost no lease-purchase (one to two percent) is used to finance state buildings (except prisons). Only one building has been a lease purchase. Since 1983 the state has used bond financing almost exclusively, including for universities and community civic areas. A separate entity called the state Building Authority sells the bonds. The cap is \$1,350,000,000 and all of this has been used. Some of the bonds are currently being paid off.

No needs assessment exists for upgrading older office buildings in the capitol area. The state keeps track of the progress of authorized projects. It has an outdated list of all buildings, but it is incomplete and is currently being updated. The state does not have a general asbestos abatement policy. It is reluctant to get involved in abatement, although it has surveyed all buildings and will do abatement on a case by case basis.

State of Minnesota

About ten years ago Minnesota conducted a master plan study, but never took any action. Currently a state task force is compiling information for a study of space and financing issues regarding state offices. It has conducted many studies and provided literature to the task force. The state has a 1988 policy considerations report called "State Office Space: Options and Cost," which explains the policy, costing assumptions, the automated prospectus system usage, etc.

The state does not have a written outline of the process used to plan and build new state office space. Generally, the Real Estate Management Division handles it by making the leasing arrangements, programming the needs, etc. The Division cannot authorize construction, but must go to the Legislature to request funds. The process generally is to obtain approval for each phase of the process from planning to construction.

The last major construction of a state building was done in 1967. Currently the state is building a new judicial center to house a courtroom and other administrative functions; it will be completed in late summer of 1990. Generally, the process to build takes approximately six years. In the capitol complex area, the state must undergo "design competition" which lengthens the process.

Currently, the state owns 1.5 million sq. ft. of space and leases 2.0 million sq. ft. Although the amount of leased space has been increasing, the Real Estate Management Division is trying to convince the legislature to increase the amount of owned space. Since 1984, it has been consolidating agencies to become more efficient. However, the amount of leased space continues to increase.

For new or remodelled office construction, the Real Estate Management Division uses straight appropriation that is 100 percent bond financed by the legislature. The state would like to start using lease purchase, in accordance with the draft report recommendations.

Minnesota has a list of all state buildings, but it does not provide a basis for determining needs, or maintaining records about needs. The state formulates space plans as needs arise.

Minnesota has a policy to remove asbestos from older buildings that are being remodelled and from any building where the presence of asbestos is a clear danger. It does not have a policy to remove asbestos from all buildings. The state has done a couple of surveys in the past and are in the process of updating them.

State of Missouri

Missouri is currently working with a consultant on a facilities master plan. In the past, the state has had problems with agencies unwilling to accept the decisions of the Leasing Department. The master plan will determine the exact requirements of every department; it will be completed in late 1990 or early 1991 and has been in progress for the last year. The judicial and legislative functions will not be included in the plan, but according to the state, the executive branch represents "99 percent" of the problem. Missouri is also in the process of updating their state regulations.

Missouri has a written outline of the process used to plan new office space for leasing. The agency must fill out a form which justifies space needs, personnel and other requirements. Then the Leasing Department holds a competitive bid for a one year lease. At the end of the year, the bid process is repeated.

The last new state office building was completed in 1983 (the Truman Building). In 1987 the state remodelled one building. Presently it is constructing a State Records Center, which will cost approximately \$18 million. The length required for new construction from initial planning to actual occupancy is approximately five years. For leased space, the process takes approximately three years, and because of this, space needs have been met through leasing.

Approximately 40 percent of the state office space is leased. The state has been leasing on a competitive bid basis and have a one-year lease limit with five- to ten-year renewable options to purchase. Usually the state does not choose to purchase, but a renewable option is needed so the state can determine the property's worth. Leasing has been expanding, but the rate of expansion has been steady. All leases begin July 1 and end June 30.

All agencies must go to the General Assembly for funding. Only one state building has been lease purchased. There is opposition to lease purchase because it is incurring state debt without taxpayer approval.

Missouri does not have a master list of facilities.

It is the state's policy to not occupy buildings with asbestos. Also, the state has strict handicap and life safety codes which bidders must meet as well as restrictions with regard to ventilation and HVAC. Bidders must submit two bonds:

1. Bid Bond - which is placed when they bid. Full architectural drawings must be produced 45 days after the project begins. If a bidder fails to do so, the state keeps the bid bond. The drawings are reviewed by a state engineer to ensure that they meet the stringent codes.
2. Performance Bond - before occupancy, the state will send an engineer to inspect the building. If the building doesn't meet the design specificities, the state keeps the performance bond.

The state implemented this strict process in the last year. It required increased staffing, but ensures that contractors perform duties as specified in their contracts.

State of New York

New York has a facilities master plan for state office space and a centralized space planning approach compared to other states. The Department of Space Planning in New York has 30 persons. The Lease Office handles leased space and lease purchase and is Space Planning's "sister office." The master plan is annually updated through funds from the current fiscal year. The department has a data base with an inventory of all state-owned space.

Those requesting space changes must complete a standardized form which asks for information such as a list of personnel, furniture, or other space requirements. They have on computerized file the space requirements of all of its client agencies. This includes almost all agencies, except the Department of Education. A fiscal inventory is conducted to determine if agency requirements match those submitted in the request form.

Requests for space are submitted to the Department of Space Planning which establishes square foot requirements. Initially, it is determined if the needs can be handled in existing state-owned space. If not, contact is made with the Lease Office which prepares alternatives. Space Planning processes the space plan and approves it, but does not have direct fiscal control. This is handled by the Division of the Budget which prepares the budget for the legislature. Fiscal approval is more administrative than legislative.

There are a number of projects currently underway: a 100,000 sq. ft. building that is a rehabilitation of an old factory; a "turnkey" project which will take two years from request to occupancy; and a 450,000 sq. ft. lease purchase agreement for an Environmental Conservation building which will take three years from request to occupancy. Generally, it takes two to four years from approval to occupation, depending on the location. (For example, in New York City, the process four years. In upstate New York, it takes less time.)

Currently the state has a total of 23 million sq. ft. of space. Of that, 12 million is owned, and 11 million is leased. The state has been increasing the amount of leased office space due to the growth of governmental agencies, as the table below shows (in million of sq ft):

1985	8.1
1986	8.6
1987	9.1
1988	9.7
1989	10.2
1990	11.2

At the same time, the amount of owned space has not changed substantially.

Most construction projects are financed by the county where the building will be located. The state then makes payments to the county until it the balance owed is paid in full. Last year, the legislature approved 25-year lease purchase agreements. The state pays higher amounts for the 25 years but it can eventually own the building, saving money in the long run. The state wants to do more lease purchase agreements. Since approval, four projects have been authorized with such an agreement.

There is a state policy for asbestos abatement; older buildings have been surveyed and are abatement criteria established by the Health and Safety Office are being followed.

State of Ohio

There are a number of agencies responsible for planning for state office space, but there is not a single comprehensive master plan in the state of Ohio. The Ohio Building Authority (OBA), which is a quasi-governmental agency, has a 20-year plan, including building needs assessments, that is updated every two years to include information on the buildings that were constructed in the interim. Thus far, a total of five buildings have been constructed statewide, two in Columbus.

To obtain space, the requesting agency must first go to the Department of Administrative Services, and then to the legislature for approval. If the project is approved, then it is given to the OBA to fund. This sequence takes approximately four years, but can be longer if a building's design and function are special or unique.

The state does not have any agency that determines the proportion of leased versus owned space. The general policy is to avoid leasing space and to place agencies within state-owned space. However, the amount of leased space has been increasing.

The OBA uses only tax-exempt bond financing for all projects.

Because most of the state office space is newer, there are few problems with asbestos. However, the general policy is to abate whenever asbestos is found. The James A. Rhodes State Office Tower, a 41-story, 1.1 million sq. ft. building constructed in 1974, was abated in 1986. All buildings have been surveyed.

State of Washington

Washington has a facilities master plan that was written in 1982 and is currently being updated. This is the first update, and it is being supplemented with Thurston County's master plan. It includes all functions.

The state does not have a written outline of the process that is used to plan and build new state office space. The Thurston County master plan, however, does. Currently the state is involved in a four building program that began the planning phase in August of 1988. This program includes:

1. Three Natural Resources agencies, \$73 million (will be located in capitol campus)
2. Department of Labor, \$63 million (will be located in Tamwater, near Olympia)
3. Department of Ecology, \$53 million (will be located in Lacey, near Olympia)
4. State Patrol, \$60 million approximately, still in the planning phase

The length of time it takes from initial planning to occupancy varies since it is dependent upon funds and legislature approval (e.g., in the mid-70s planning was done for Natural Resources building, but funding was never approved, so it was never built). The current program for the first two buildings started in 1988 and completion of construction is scheduled as follows:

1.	Natural Resources and Department of Labor	1992
2.	Department of Ecology	1993
3.	State Patrol	1994

Programming can take anywhere from four to seven years. The current program is handled by a Design/Build Procurement, in which the private contractor is responsible for both design and construction.

Currently, about 50 percent of state office space is owned and 50 percent is leased. State ownership of space is favored. General Administration has recently convinced the legislature that it is cheaper to own than to lease, based on life-cycle planning. The decision to lease office space depends upon the growth of the governmental agencies.

For the Department of Ecology, Certificates of Participation were used to fund the project. For the State Patrol, gas tax money was used. The state's key concern is to not dip into the general fund because the legislature does not want to take away any money from higher education or prison construction. The state agencies must devise other ways to obtain funds.

The state has a needs assessment for upgrading older office space. Upgrading is done on a case by case basis. The state has a policy to survey and remove asbestos; surveys have been conducted, but not all asbestos has been removed.

APPENDIX B

OPDM PLANNING PROCESS

The current methodology that OPDM uses for deciding the location of state offices is a four-step process that includes a survey of existing conditions, a forecast of staffing and facility needs, a derivation of alternatives, and recommendations. After an agency or department has completed an internal planning process to identify needs, the department prepares a conceptual plan. The department may do this plan internally, may approach OPDM for assistance (although this is not required), or hire a consultant for this phase. If OPDM assists in the Facility Master Plan and Concepts phase, location will be one factor considered in a conceptual plan. The following describes the process as performed by OPDM.

1. Survey of Existing Conditions

The survey of existing conditions includes a description of the existing facility location detailing age, condition and size of the facility. This provides the square footage of the floor area and other configurations useful for determining space needs of a given department. Square footage for special space needs is also described for space currently used for other than regular office space; for example, public reception area, conference rooms, records and files, copy area, mail equipment and counter area, unit equipment (e.g. microfilm viewers, etc.), computer room. These will vary from agency to agency.

The tenure of the agency in the existing space is documented, noting whether the office space is owned or leased as in a lease-purchase agreement. This information is important for determining the alternatives open to the requesting agency and for developing financing options available to the agency.

The survey of existing conditions also describes current transportation, parking, and access requirements for visitors, clients and staff, and the average number and variation of visitors per day are estimated from historical records. A comparison of the need for parking and the availability of parking is based on an estimate of visitors and a description of the number of parking spaces available. The commute modes of the employees are examined to determine whether the current location is accessible to public transit. The survey of existing employee commute modes provides important transportation information in determining the location of state office space.

The description of the program and its responsibilities are fully detailed, including the number of units, functions, organizational chart and staff allocation (full-time, part-time shifts). This information provides planners with a realistic view of the space being requested and how it is to be utilized.

2. OPDM's Current Forecast Staffing and Facility Needs Methodology

An analysis of the effectiveness of OPDM's methodology is presented in the body of the report. This discussion is intended to briefly summarize the process. The forecast of staffing and facility needs is a quantification of current staff and square footage of the facility currently in use. It is a five and ten year projection of staffing and a calculation of corresponding total space demand given special space needs of the requesting agency.

The assumptions used in estimating the staffing demand are clearly stated. For example, is staffing demand expected to remain constant in the next two years or is it expected to grow or decline? If growth or decline is expected, by what proportion? What is expected to happen in five years and what can be projected for ten years? The changes in dynamics of the internal operations of the requesting department, which is the driving force behind the staffing demand, is detailed. This provides the clue as to the source of the demand for space.

At this stage of the planning process, basic space demand is usually calculated using a standard of 150 net square feet per employee. Calculations for special space needs unique to the requesting agency are added to this minimum amount to determine the total facility space demand. This calculation establishes a base which is refined later to prepare a more specific space program. It is the later space planning program which ultimately will conform to the guidelines in the State Administrative Manual. (Section 1402).

Finally, to determine the final size of the required facility, given staffing demand for corresponding years (five, ten years), 25 percent of the space demand is added to the total. This proportion is allocated to building circulation, major hallway, elevators, and stairways. Restrooms, mechanical, electrical and telephone equipment rooms are added as tare.

3. Generation of Alternatives

The generation of alternatives usually will consider "do nothing," "relocate," "lease," and "acquire" and perhaps variations of. The following criteria are used to determine the viability of a given alternative: program needs; location needs; financing and cost; existing plans; building size requirements; consolidated or split operations; access, parking, and transportation issues; environmental issues and required documents; external political and economic factors; and timing and scheduling of procedural steps.

The ranking of the alternatives based on the rating scheme is subjective, given the fact that only one of the criteria (cost in dollars) lends itself to a unit of measurement. The others are nominal factors which raise all the old issues of who decides what the ranking should be and how the decision should be made. For example, using the accessibility criteria, it is understood that ideal is more desirable than good and good more desirable than fair. What is not known is whether the desirability expressed between ideal and good is the same distance as that between good and fair. To complicate matters, is accessibility more important than location needs and vice versa?

Although it is not clear how this ranking is done, at least the criteria and the rating scheme are presented in the alternatives section to show how each alternative is rated. It is plausible that the particular planner responsible for a given study is the one who decides on the importance of the criteria and the ranking of the rating scheme subject to review. This leads to the conclusion of a non-standardized method for generating alternatives.

4. Recommendations and Actions

The recommendation and actions present a description of the preferred action; that is, what to do -- build, buy, lease, or other and where. A recommendation on how to finance the preferred action is also provided. The justification for the preferred alternative is detailed,

giving the rationales for that choice. Finally a description of the second choice strategy is presented for comparative reasons and as a fall-back position.

OPDM, in the context just discussed, considers appropriate criteria for deciding where a department should be located. However, the current method and process described for locating state office space in Sacramento by OPDM is done only within the framework of a feasibility study, usually for the purpose of choosing between specified alternatives. The process is a "piecemeal" approach which deals with one case at a time in isolation. That is, OPDM responds to the location needs of a requesting agency as a service agency.

Consultants recommend that the state should develop a systematic planning process for locating state office space in Sacramento. This implies placing authority of the planning function within an agency whose role will be to see that the objectives of the CAP are achieved.

APPENDIX C

CAPITAL OUTLAY PROCESS COMPONENTS & TIME LINE

- I. Concepts and Documentation Phase (Facilities Planning)
(2-5 months)
 - A. Project Initiation, Concept Development by State Agency
 - B. Preparation of Facilities Plan and Supporting Data
 - 1. Planning Assumptions
 - a. Desired Location (e.g. remain in Sacramento)
 - b. Ownership (e.g. own its facility)
 - c. Funding (e.g. purchase through C.O. Process)
 - d. Availability of funds (e.g. funds are available)
 - 2. Survey of Existing Conditions
 - a. Program of Agency
 - b. Facilities Inventory
 - c. Employee Population
 - d. Employee Travel Characteristics
 - e. Visitor and Parking Demands
 - 3. Forecast Employee Population and Space Demand
 - 4. Financing Options
 - a. Leasing
 - b. Lease with Option to Purchase
 - c. Lease/Purchase
 - d. Ownership
 - 5. Alternatives, Analysis and Evaluation
 - 6. Recommendations and Actions
 - C. Approval of Facilities Plan by DGS and client state agency, if appropriate
 - D. Preparation of Five Year Program and Capital Outlay Budget Change Proposal(s) (COBCP's) by state agency.
 - 1. Five Year Program
 - a. List of projects planned, with estimated costs in priority order
 - b. List of criteria used to determine project priority
 - c. Discussion on how each project meets these criteria
 - d. Discussion of alternatives for financing plan
 - e. Recommendation for financing the plan, based on one or more of the alternatives.
 - 2. COBCP's
 - E. Summary Sheet listing all proposed projects in departmental preliminary priority order
- II. Budget Package (BP) Phase (17 months)
 - A. COPBCP sent to Department of Finance (DOF) and OPDM
 - B. DOF and OPDM review of COBCP for budgetary implications, clarity of scope definition, technical feasibility of the proposal, appropriateness of cost estimates, discussion on alternatives
 - 1. If DOF approves, go to "C"
 - 2. If DOF rejects, COPBCP returned to Agency for either rejection, rewrite, revisions, or additional information
 - C. DOF asks OPDM for fee to do BP
 - D. OPDM requires fee proposals to do BP from:
 - 1. OSA, or if workload, time restraints, or complexity require

- 2. Outside private consultant
 - E. OPDM receives fee proposal, informs DOF of amount and requests approval from DOF to proceed with BP preparation
 - F. If DOF approves, OPDM authorizes preparation of BP
 - G. BP is prepared including scope, pre-schematic drawings, cost estimate, outline specifications, schedule
 - H. OPDM reviews BP for general consistency
 - 1. If not acceptable, returned for revisions, or corrections
 - 2. If acceptable, sent to DOF
 - I. DOF conducts scope meetings and budget hearings with client agency, OPDM, LAO
 - J. Governor's Budget is prepared by DOF using data in BP; Legislative Review/Hearings are held during the Spring
- III. Land Acquisition Phase (0-12 months)
- A. Department and OREDS begin site selection process
 - B. After site is identified, report is prepared for Finance by OREDS
 - 1. Description of property (e.g. acres, assessor's parcel numbers)
 - 2. Specific location including vicinity map, Senate/Assembly district numbers, parcel numbers, "Zone of Interest Map" showing proposed and currently acquired areas.
 - 3. Purpose of acquisition
 - 4. Potential use of existing facilities
 - 5. Factors influencing site selection
 - 6. Approximate value of each parcel
 - a. Basis of appraisal
 - b. Proposed funding source
 - 7. Funding history, priority of project compared with department's Five Year Plan
 - C. PWB approves site selection
 - D. OREDS acquires property
 - E. PWB approves settlement price
- IV. Preliminary Plans (PP) Phase (3-12 months)
- A. Consultant Selection Process (see Appendix)
 - B. Prepare PP's (which can include initially Schematics and then moving onto Design Developments (DD) Documents or just DD's)
 - 1. Plans
 - 2. Specifications
 - 3. Estimate
 - C. Review PP's
 - D. Public Works Board (PWB) approval of PP's and authorization to proceed with Working Drawings; request due to PWB 20 days before scheduled meeting unless legislative notification is required; then, 25 days before scheduled meeting
 - E. Department submits Forms 14D and 22 to DOF to encumber funds for Working Drawings.
- V. Working Drawings (WD) Phase (3-12 months)
- A. Consultant Selection Process, if required (see Appendix)
 - B. Prepare Plans, Specs., Estimates (PS&E) (which can include 50, 75, and 90 percent completed documents)
 - C. Review of PS&E
 - 1. Plans and Specifications

- a. Review by OPDM and other state Reviewing Agencies (e.g. State Fire Marshal, Structural Safety Section of OSA, Office of Statewide Health Planning and Development (OSHDP), where required
 - b. Make revisions, final checks and final review
 - c. Certify OSHDP, if necessary
 - 2. Estimate
 - a. Review by OPDM
 - b. Update if necessary
 - c. Prepare final estimate
 - d. Request Accounting to certify availability of funds
 - e. Combine and submit SAM 6722 data to client agency
 - i. Complete and dated set of ED's, specs and final cost estimate
 - ii. Form 14D, "Request for Approval to Proceed or Encumber Funds"
 - iii. Updated project schedule
 - iv. Certification that the scope of the project is the same as the legislatively approved scope
 - f. Submission of data (per SAM 6722) by client agency to DOF
 - g. Review of data by DOF
 - h. DOF approves notice to proceed (Form 14d) to bid the project
 - J. Notifications
 - 1. Assembly members of project's district
 - 2. Senators of project's district
 - 3. Board of Supervisors/City Council of project area
- VI. Bidding Phase (3-6 months)
- A. Advertising
 - 1. Prepare advertisement
 - 2. Prepare advertisement schedule; submit to OSA Specification Section and after reviewed, to Contracts Section; submit ad to trade and general circulation papers and State Contracts Register
 - 3. Specifications submitted to Spec. Sect., reviewed, print specs
 - 4. Stamp plans "Released to Bid," submit to OSA, coordinate plans and specs, print and assemble plans
 - 5. Issue plans and specifications to interested parties, builders exchanges and minority plan rooms
 - 6. Verify contractors pre-qualifications
 - 7. Issue bid proposals
 - 8. Answer various bid questions
 - 9. Answer and resolve requests for clarifications from contractors
 - 10. Conduct pre-bid conferences
 - 11. Perform Minority Woman-owned Business Enterprise MWBE outreach
 - 12. Issue addenda, as necessary
 - B. Award of Contract
 - 1. Receive bids
 - 2. Analyze bids
 - a. Check licenses
 - b. Check Small Business Preferences
 - c. Check pre-qualifications

3. Distribute bid tabulations
 4. Prepare financial statement
 5. Resolution of any errors in bid
 6. If bid is over appropriation for construction, augmentation will be required. PWB can authorize augmentation up to 20 percent. Any single augmentation or aggregate augmentations that exceed 10 percent of the funds appropriated require a 20 day notification to the Joint Legislative Budget Committee
 7. Approve to award (14D)
 8. Certification of SMWBE Goals or Good Faith Effort
 9. Transfer of funds
 10. Obtaining signatures including bonds and insurance
 11. Issue Notice to Proceed
 12. Obtain any substitution of subcontractors
 13. Certify payroll requests from unions and Dept. of Industrial Relations
 14. Prepare and submit necessary quarterly reports
- VII. Construction Phase (3-36 months)
- A. Kickoff meetings
 - B. Construct project
 1. Monitor construction progress
 2. Monitor schedule
 - C. Progress payments
 - D. Process Change Orders (a change to contract)
 - E. Close out contract
 1. Final inspection
 2. Punch list
 3. Warrantees and guarantees
 4. Keys and manuals
 5. Acceptance of contract
 - F. Resolution of contract time and assessment of liquidated damages (if appropriate)
 - G. Notice of Completion or Cessation filed with County Recorder
 - H. Proposed final payment
- VIII. Claims and Close-out Phase
- A. Contractor files claims
 - B. Resolution of claims
 - C. Arbitration
 - D. Final payment
 1. Existing funds
 2. Augmentation
 3. Board of Control
 - E. Return balance of funds
 - F. Close contract and project number per G.C. 14959
- IX. Environmental Review Process Phase (must be completed before PP's are completed and state agency goes to PWB) (4-24 months)
- A. Project Initiation
 - B. Project Description
 - C. Initial Study
 - D. Notice of Preparation
 1. Preparation

- 2. Review Period
 - 3. Scoping Meeting(s)
 - E. Draft Environmental Impact Report (DEIR)
 - 1. Preparation
 - 2. Administrative DEIR (ADEIR) production
 - 3. Initial internal review of ADEIR
 - 4. Incorporation of internal review comments
 - 5. DEIR production
 - 6. Public review of DEIR
 - F. Final Environmental Impact Report (FEIR)
 - 1. Scoping of comments
 - 2. Preparation of responses to comments
 - 3. Preparation of Administrative FEIR (AFEIR)
 - 4. Initial internal review of AFEIR
 - 5. Incorporation of internal review comments
 - 6. FEIR production
 - G. Statement of Findings, Certification, Notice of Determination, Statement of Overriding Consideration
 - 1. Preparation of Statement of Findings (SOF)
 - 2. Preparation of Certification (CERT)
 - 3. Preparation of Notice of Determination (NOD)
 - 4. Preparation of Statement of Overriding Consideration (SOC) (if required)
 - 5. Review of SOF, CERT, NOD and SOC (if required)
 - 6. Signing of SOF, CERT, NOD, and SOC (if required)
 - 7. Filing of NOD
 - H. Litigation Period
- I. Consultant Selection Process
 - A. Define scope of project for advertisement in State Contracts Register (SCR)
 - B. Place ad in SCR and professional publications for Statements of Qualifications
 - C. Review Statements of Qualifications
 - D. Determine SMWBE Goals met or good faith effort performed
 - E. Determine short list of qualified consultants
 - F. Notify short listed consultants of interviews
 - G. Conduct interviews, including scheduling and notification
 - H. Make selection of consultant and notify
 - I. Request proposed fee schedule from consultants
 - J. Prepare estimate of value of services (EVS)
 - K. Agreement on scope and then fees with consultant
- II. Contracting Process
 - A. Prepare agreement
 - B. Send to consultant for signature
 - C. Obtain necessary approvals
 - D. Issue Notice to Proceed to consultant
 - E. Prepare and submit required quarterly reports

APPENDIX D PROJECTIONS

A. CURRENT PROJECTION METHODOLOGY

1. OPDM's Projection Methodology

A facilities plan must answer the difficult question of how large each facility must be several years into the future. Because space is a function of staff size, planners generally project staffing levels first and then translate these into square footages.

At the level of the Facilities Plan, OPDM conducts an annual survey of the department heads or business services officers and uses their expectations of 5- and 10-year growth for its staffing forecasts. If an estimate does not exceed a "normal" rate of growth it is accepted without modification; otherwise the planner goes back to the agency to discuss the reasons for the rapid increase. The final figure is agreed upon by both parties; OPDM does not dictate the answer.

This very simple procedure may be the most practical technique for a preliminary estimate of the growth of a large number of agencies when only a very small planning staff is available. But how well does it work? Since the first survey was conducted in 1977 it is possible to compare the early predictions with the actual staffing in later years. To put this into context, general trends in state employment and the data available to evaluate the forecasts are discussed first.

2. Trends in State Employment

The growth of public agencies is affected by a host of external factors. Other things being equal, staffing grows along with state population, perhaps slightly more slowly because of increasing efficiency in agency operations. But shifts in public demands and socioeconomic conditions can substantially modify these growth patterns by adding new responsibilities or curtailing old programs. The California tax revolt, and specifically the provisions of the Gann Amendment, have attempted to place limitations on overall growth, though there was a hint in the June 1990 primaries that this may be relaxed somewhat in the mid-term future.

The current study, however, is concerned primarily with those employees in Sacramento rather than statewide. Sacramento employees will not necessarily follow the same growth pattern as the total. There has been strong growth in some programs in the capitol, particularly prison construction and toxic waste management, which has caused corresponding increases in Sacramento employees. Proposition 13 caused a shift in responsibilities from the local to the state level, and it has been suggested that this may also have contributed to the growth of state employment in Sacramento. Developments of this sort will have important consequences for the Sacramento Facilities Plan.

3. Data from OPDM and Other Sources

Aggregate data are available for historical and current state population, total state employment, and office population in the Sacramento area. The first two of these come from the 1990-91 Governor's Budget. Appendix Figure 1 below shows the growth of total state government employment, and Appendix Figure 2 shows this figure per 1,000 state residents since 1958. Total employment has increased nearly every year, but per capita employment hit its peak in 1977 and declined steadily until 1988.

Figure 1
California State Employees
Statewide, Total

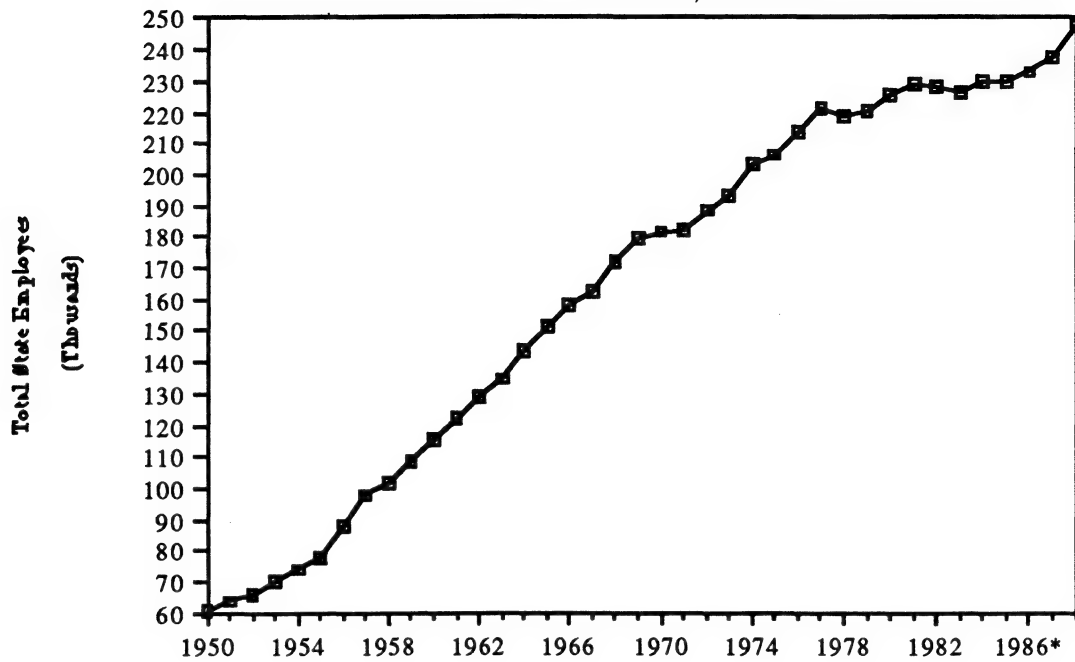
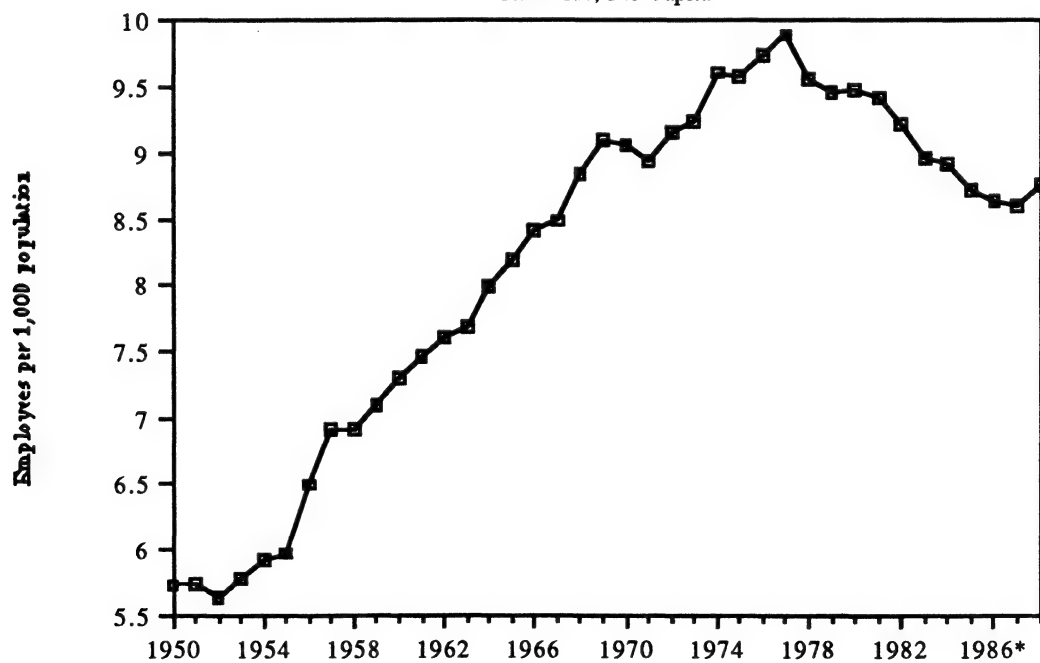


Figure 2
California State Employees
Statewide, Per Capita



*Staffing estimated: 1983, 1986, 1987.

OPDM (and its predecessor, OFPD) made current and predicted staffing surveys for 1978 through 1982, calculated Sacramento-area totals for 1984 and 1985, and conducted another full survey in 1988. The five- and ten-year predictions for the earlier period can be compared with the actual staffing in the later years. Table 3 shows the total staffing for 1977 to 1988 (data for the starred years are Consultants' interpolations), as reported in the 8th Supplement to the Sacramento Facilities Plan.

Table 3: OPDM Space Data¹

Agency	Year	NSF		Now	Employees	
		Office	Other		5 years	10 years
EDD	1978	284,848	55,130	2,286	2,489	2,665
	1980	623,860	55,130	4,010	4,514	4,907
	1982	630,180	67,850	3,949	4,151	4,403
	1988	713,201	NA	4,479	4,552	4,629
DMV	1978	623,256	68,763	4,219	8,749	9,567
	1980	624,160	68,760	3,859	3,901	4,001
	1982	624,200	72,400	3,543	3,951	4,001
	1988	608,154	NA	3,079	3,420	3,762
CALTRANS	1978	367,158	195,316	2,265	2,491	2,591
	1980	328,280	241,310	2,640	3,004	3,004
	1982	366,850	241,700	2,745	3,057	3,057
	1988	591,981	NA	2,864	3,125	3,327
FRANCHISE TAX	1978	371,243	51,598	1,872	2,193	2,454
	1980	371,230	112,600	2,726	3,456	3,901
	1982	516,610	NA	3,667	4,124	4,746
	1988	624,714	NA	2,714	4,256	4,872
HEALTH SERVICES	1978	NA	NA	1,525	1,708	1,872
	1980	294,760	51,400	2,170	2,392	2,622
	1982	291,068	51,400	2,466	2,703	2,978
	1988	420,296	NA	2,497	2,788	2,968
GENERAL SERVICES	1978	241,504	488,741	1,624	1,780	1,880
	1980	242,000	626,460	2,110	2,284	2,515
	1982	397,720	605,351	2,126	2,200	2,229
	1988	464,110	NA	2,043	2,163	2,274
SOCIAL SERVICES	1978	403,490	16,379	3,058	1,312	1,410
	1980	260,740	23,210	1,638	1,937	2,165
	1982	277,340	70,800	1,861	1,982	2,028
	1988	337,974	NA	1,827	1,971	2,150
TOTAL, 22 largest agencies	1978	4,160,300	1,315,430	28,754	34,382	37,051
	1980	4,746,810	1,991,710	32,049	35,867	38,770
	1982	5,206,820	1,765,701	33,684	36,424	38,762
	1988	6,803,328	34,883	38,965	41,494	
less Lottery	1988	6,685,190	34,189	38,271	40,800	
TOTAL, all agencies	1978	6,083,700	NA	37,600	44,100	48,800
	1980	6,500,000	NA	41,640	46,342	50,390
	1982	7,139,100	NA	43,590	47,170	50,185
	1988	9,161,267	NA	45,815	51,421	55,244

¹In 1978 a major reorganization transferred some 1,100 employees from Social Services to EDD and another 550 from Social Services to Health. These changes were reflected in the 5-year outlook for Social Services only. The absolute growth in these three departments combined (1978 to 1988) has been 1934 new employees in the Sacramento area.

Sacramento area employment (for which the earliest data came from the original 1960 Plan and may not be comparable) shows growth similar to that of state employment overall, but the drop in per capita employment does not begin until 1982 (Appendix Figures 3, 4). In particular, it rose sharply for five years (1977 - 82) when statewide per capita employment was falling. The percentage of total state employees in Sacramento continued to increase until 1985 (Appendix Figure 5). This trend also may have reversed itself, though that will not become clear for a few more years.

Figure 3
California State Employees
Located in Greater Sacramento Area

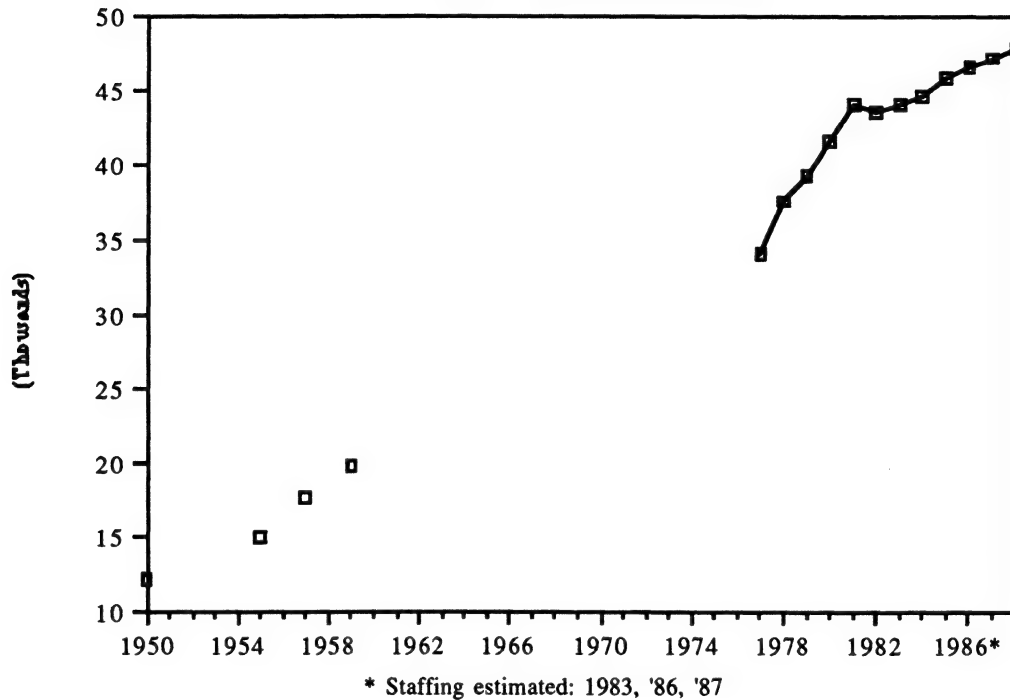


Figure 4
California State Employees
In Sacramento, Per Capita

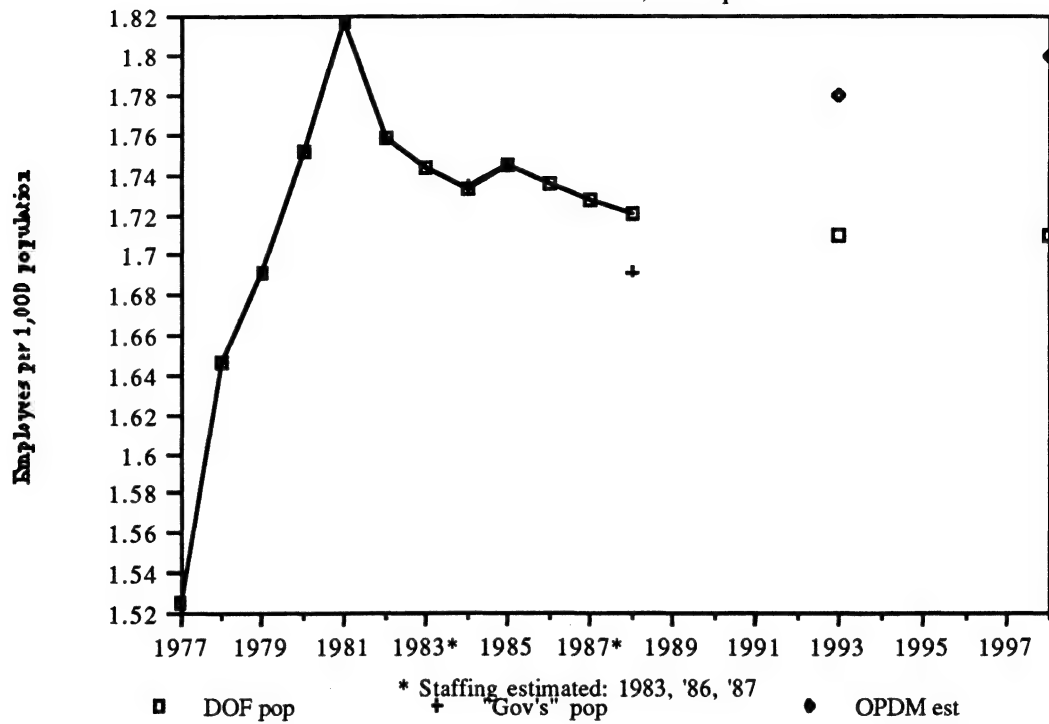
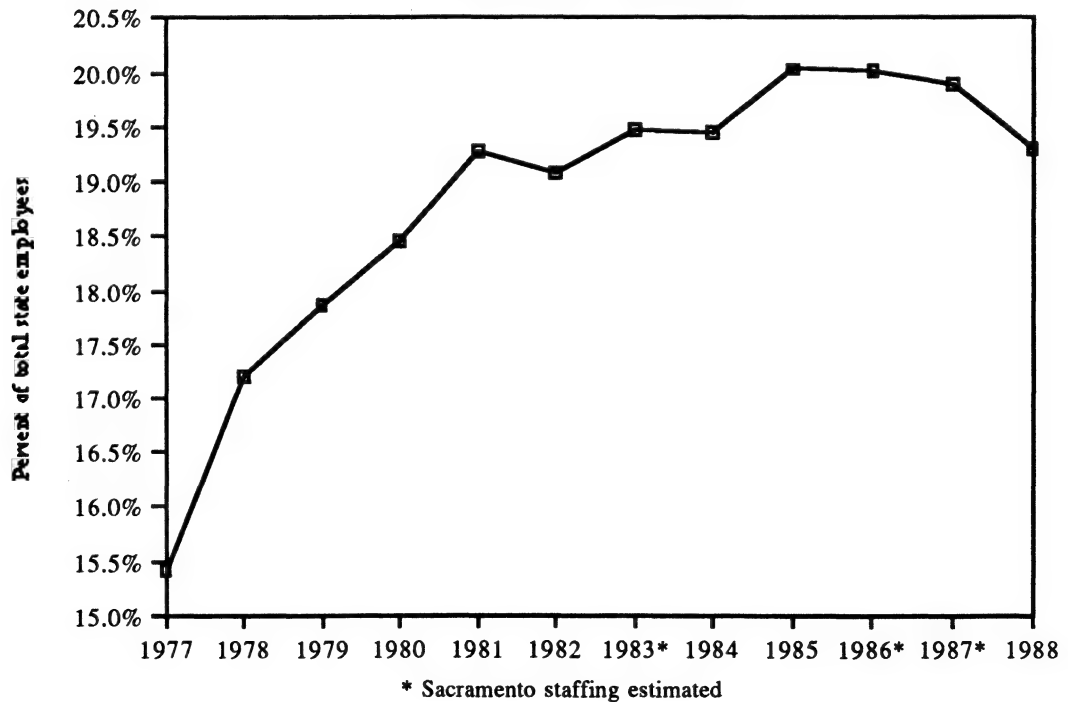


Figure 5
California State Employees
Percent of Total in Sacramento



4. Comparison of Forecasts with Actual Staffing

Most of the 5-year forecasts for total Sacramento employment (excluding the one made for 1986) were quite accurate, and even the ten-year forecast is only a little high, equaling perhaps what the staffing will be in 1990. In terms of overall demand, the rather simple methodology described above gives accurate results.

When individual departments are examined, however, it appears that this agreement between prediction and actuality may be fortuitous. Table 3 also shows the same figures for the seven largest departments, most of which have well over 2,000 employees in the Sacramento area. EDD and DMV show spectacular, and opposite, inaccuracies in their 1977 estimates. (They did, however, approach reality in the succeeding years.) CalTrans and FTB, on the other hand, did fairly well with their 10-year forecasts. Farther down the list of large departments (not shown) there are two even greater errors: the Departments of Corrections and Housing & Community Development underestimated their ten-year growth by 165 percent and 130 percent, respectively; and of course in 1978 there was no projection at all for the 700 employees of the State Lottery Commission which was established later.

It might be asked why the overall forecast is so accurate while those for individual departments are often in error. There are two reasons for this. The first is that the errors are not systematic: some estimates are too high and some are too low, so they average out. Second, it is probably the case that funding of state employment overall is rather rigidly constrained. The competition for funding among agencies becomes a zero-sum game where an increase in one department's staffing implies a corresponding decrease in the staffing of others. Since the Sacramento Facilities Plan is used to project space needs for individual departments as well as the overall demand, it would appear that the procedure needs to be modified when working at the individual project level of specificity.

5. Discussion of OPDM's Methodology

Forecasting is an art, not a science. Because of the great number of uncertainties and unpredictabilities in the factors affecting staff growth, planners must assemble as much relevant data as possible, from a variety of sources, and ultimately use their judgment in arriving at a final figure. Precise mathematical techniques for extrapolating historical data are available, but they assume that the future will continue to be like the past which is not a bad assumption in the short run in most cases, but increasingly inaccurate as time proceeds. Since state employment is fueled, ultimately, by state population growth, any projection of a rate which differs sharply from that growth must be suspect. (The principal exception would be of a program or activity which is being gradually phased out, never to reappear.)

OPDM's technique involves the planner's judgement rather than formal criteria at several points, for example, the decision as to whether the agency's forecast is to be taken at face value. For the maximum "normal" growth rate a range of two percent to five percent annually is used, with the planner's experience deciding exactly when the projection needs further review; and even then the final value is arrived at only after discussion and agreement with the subject agency.

Since OPDM uses agency management's expectations for staffing, it relies upon the forecasting techniques used by those managers. It is not known what those techniques are, nor at what level of sophistication the estimates are made, especially with smaller agencies. Some agencies prepare much more careful and reliable forecasts than others. When an agency predicts growth of some round number (say 10 or 100) for each 5-year period it appears that the estimate may be no more than an offhand guess.

Using managers' forecasts also runs the risk of incorporating their desires rather than an assessment of what is actually going to occur given fiscal and political realities. Program administrators are generally convinced of the need for their services and are aware of the funding shortfall; under these circumstances it is easy to slide over into the realm of predicting what would be needed to do the job properly, or even to exaggerating these needs in order to improve the chances for future staffing. Consultants do not mean to imply that this is occurring, only that, without an in-depth study of the particular agencies, it is impossible to be certain that it is not.

Despite the limitation mentioned above, historical staffing records are of use in making forecasts since they provide a counterpoint to managers' aspirations. If the funding process is seen as a contest between agency management, which wishes to expand, and the guardians of the resources (Department of Finance and the Legislature) which are trying to restrict expenditures, the historical staffing record may be interpreted as a measure of the agency's likelihood of success in actually obtaining its requested funding. As long as the personalities, issues, and strategies remain the same, the outcome of the struggle is not likely to be much different. (However a change in either the agency administration or the Governor or legislative leadership can render this indicator obsolete.)

Another technique which is used by OPDM to confirm their estimates, is the ratio of Sacramento area staffing to total state population. In the original Capitol Area Plan this ratio was assumed to be a constant 1.7 office staff per 1,000 residents. In the 8th Supplement this ratio was updated to 1.8 per 1,000. However, Appendix Figure 4 shows that this value was attained only in 1981; by 1988 the ratio had fallen to 1.72 and appeared to be on a steady path downward. The proportion of state employees in Sacramento has also begun to fall (Appendix Figure 5). Given the overall drop in per capita state employment it appears that future Sacramento employment may not be quite as high as 1.8 per thousand.

(Note that there are different sets of state population figures for making the per capita calculations; using a different series will give different ratios. Appendix Figure 4 was constructed using the staffing figures from the 8th Supplement and population figures from Report 88 P-4 (Department of Finance, Population Research Unit, February 1988). This will be the last set of population projections until the 1990 Census figures become available. The tail end of the curve in Appendix Figure 4 also shows staffing ratios calculated according to the "Governor's" population figures; these figures are taken from Schedule 5 of the appendix to the 1990-90 Governor's Budget, and represent later estimates by DOF. They are in close agreement with the "DOF" figures through 1985 but then become somewhat larger. The "DOF" population estimate for 1988 is 27,847,200; the "Governor's" is 28,323,000. However, only the DOF series extends beyond 1988, so it is used for the projections even though it may not be as accurate. Since Appendix Figure 4 uses a single set of population and staffing figures, it will at least be internally consistent even if the exact values differ from those in the Supplement.)

OPDM attributes the growth in the per capita ratio primarily to increases for corrections and toxic wastes. While these have indeed grown, several programs unconnected to them have also grown much faster than population: examples are EDD, the Franchise Tax Board, the Controller, Housing and Community Development, and the state Lottery, which was not there at all in 1978. The increase is due to growth in a number of programs, not just in toxics and corrections.

6. Recommended Modifications to the Methodology

How should the state make population forecasts? As argued above, as many factors as practical should be considered. These, unfortunately, require staff time. Given the resources available to it, OPDM is employing reasonable procedures for staffing projections. If more planning manpower were available, it would be useful for OPDM to supplement these forecasts with a review of historical staffing records, both at the departmental and the aggregate levels. Agency planning officers should be interviewed, particularly with regard to the acquisition of new programs or responsibilities or the phasing out of old ones, and changes of this sort should be included in the considerations.

Few responsible planners will claim a high degree of reliability for forecasts for ten or more years in a dynamic situation such as California state government. Unfortunately, state-owned buildings take nearly ten years from conception to occupancy. By the time they are built the original plan is outdated. Even if the present cumbersome funding construction process were to be appreciably shortened it would add only a few years to the usefulness of the plan. This then becomes an argument for building flexibility: allow rearrangement of interior space, make provision for addition to the building, and consider general-purpose buildings suitable for several agencies.

B. CONSULTANTS' STAFFING ESTIMATE

Consultants have made an independent projection of total Sacramento area office staffing. The model begins with the staffing as of 1988 (the latest year of the survey) and makes the following assumptions:

The population of California will grow from 27,847,200 in 1988 to 30,116,600 in 1993 and 32,111,700 in 1998

Per capita staffing in Sacramento will continue to decrease for a few years, from 1.72 in 1988 to 1.71 in 1991, and then level off at that value for a few years under a somewhat less fiscally conservative state administration. Since the per capita trend has been on a fairly steady downward course for seven years, it looks as though this will continue. The shortfall in the 1990-91 budget would seem to argue for the lower staffing levels at this time.

The following values emerge:

Table 4
Comparison of OPDM and Consultants' Staffing Estimates

<u>Year</u>	<u>OPDM</u>	<u>Consultants</u>
1993	53,747	51,499
1998	57,812	54,911
2003	57,910	

Using the DOF population projections, OPDM's forecasts correspond to a ratio of 1.78 in 1993 and 1.80 in 1998. These values are a little higher than the historical record of the last few years. To put these projections in perspective, note that OPDM's staffing projection for

1998 would be reached with a ratio of 1.71 in the year 2003. (Consultants are not proposing to extend their projection that far into the future.)

Any forecast must be continually updated to take account of changing conditions. The results of the 1990 survey should be inserted into this model as soon as they are available.

Making a projection for an individual agency requires an in depth understanding of that agency's needs, the fiscal and political hurdles they need to overcome, and prospective changes in both procedures and responsibilities. Obtaining such information is outside the scope of the present contract; for this reason, Consultants have not made projections at the agency level.

C. SPACE REQUIREMENTS

Translating staffing to space requirements can be straightforward or complex. In its overall estimates, OPDM takes the present space and then uses a nominal figure of 150 net square feet (sq. ft.) for each new person added. This is not a bad guess for a first approximation for office workers, though it can be far off for blue-collar staff. Consultants find that current average space use in the offices covered by the plan is 200 net sq. ft. per worker. This includes not only personal work space but an allowance for common areas - conference and break rooms, reproduction, libraries, reception, etc. The marginal figure of 150 sq. ft. takes into account, but does not increase, these common areas. For small staff increases this will not be a bad guess, but if there is substantial growth then there must be common space added as well.

When an agency's needs are examined in more detail, differences emerge. The amount of space devoted to records storage varies. Some classes of personnel (attorneys, counselors) need more privacy than others (clerks, analysts) and will thus require private offices rather than open workspace. Some agencies have special needs (libraries, laboratories, large computers). Nearly everyone would like more conference rooms and employee break areas. These can be determined to some extent from an agency's present space usage. However, existing configurations, especially in older buildings, may be determined by inefficient layouts and indicate need for more space than would be necessary with a proper design.

The use of a nominal 150 sq. ft. is useful for preliminary planning, but a detailed program for a new facility must take into account the organization's specific operations. In calculating the requirements for leased space, OREDS asks for a projection of the total number of workers by state personnel classification, and then applies the space allowances specified in the State Administrative Manual for each category, adding in common area as needed. This would be a better way to determine space requirements in the Facilities Plan overall, but takes more staff time than is available for OPDM at present.

D. COMMENTS ON THE DATA REQUIREMENTS FOR PROJECTIONS

All projections, and indeed any intelligent application of the Sacramento Facilities Plan, depends upon having a complete and accurate set of data from which to work. Some inconsistencies in facility size in previous reports have led to embarrassing errors. (See note to Table 2 in the Eighth Supplement.) In addition, the Sacramento employment figures are derived from surveys, to which response is voluntary, and for which there have been some inaccurate or incomplete responses. For example, the Legislature, which has

exempted itself from its Plan, has given at most only partial responses to the surveys, and has not been consistent in these from year to year; the resulting uncertainties appear to be the largest source of error in the current staffing figures.

What must be known, at a minimum, is the number of facilities, their size, staffing, and ownership status. Determining this is not a simple task as there is no existing compendium of this information. The Statewide Property Inventory now being compiled by OREDS is the closest approach to such a comprehensive data source. Consultants believe that this effort should continue to be supported and that this inventory should be the basis on which all facilities planning is carried out. The maintenance of a separate database can only lead to confusion (as well as being a duplication of effort.)

Database owners generally guard their property jealously and resist allowing others to make entries into it, lest it become corrupted. However, database users sometimes have access to more accurate data, and frequently need to add some of their own information. Without specifying here the exact organizational arrangement under which this should be done, Consultants recommend that OPDM use only the Statewide Property Inventory (SPI) data for their analyses and projections. This means that they must have continual read-only access to the SPI and be able to transmit updated or additional information to the SPI managers for input.

APPENDIX E

REVIEW OF OPDM'S ECONOMIC FORECASTING MODEL

INTRODUCTION

This appendix reviews OPDM's Economic Forecasting Model (EFM) from a functional and technical perspective. The functional review assesses how the model is currently being used by OPDM and others in the office space decision-making process (both lease and build). The technical review includes an evaluation of the way in which the model variables interact, such as the calculation of 50-year bond financing costs. In addition to general structural considerations is an evaluation of the parameters OPDM currently uses for the model variables, such as bond interest rates and a discussion of how the accuracy of the model may be improved by changing some of these parameters. Finally, the recommended improvements of these parameters are related to the recommended financing techniques discussed in Appendix G.

FUNCTIONAL REVIEW

The EFM is used as an analytical tool by OPDM to assist in office space financing decisions. Broadly speaking there are two general types of financing approaches used by OPDM to accommodate office needs that are incorporated in the EFM: private and public. The private options include straight leasing of privately owned buildings and variations of lease/own, such as lease with an option to purchase and installment sale. The public financing approaches use either Capital Outlay Funds or a form of tax-exempt financing, such as lease revenue bonds or certificates of participation to raise money for constructing an office building.

The EFM can evaluate the financing parameters within a single technique, such as straight leasing, or compare two different financing approaches, such as straight leasing vs. lease revenue bonds. For example, it can evaluate two different base rent assumptions for a lease OREDS is negotiating. For the same negotiations, OREDS may want to compare a straight leasing approach with a lease-purchase option. Although it can be used to assist in leasing negotiations, the model is primarily used for OPDM planning purposes.

The model must be flexible in order to analyze, at different levels of detail, the economic trade-offs of private vs. public financing options at different points along the space planning process continuum. This means that it must contain a sufficient number of variables that can interact to provide results at all stages of the Capital Outlay Process; i.e., from conceptual planning and budget preparation through working drawings and the bidding/construction phase.

Consultants found that the number and types of variables included in the model were sufficient to carry out this mandate. The following list of the types of variables contained in a hypothetical straight lease vs. build comparison evaluation illustrates the comprehensiveness of the EFM.

Straight Leasing Variables

- Building life
- Estimated annual operating and maintenance (O&M) costs
- Date of O&M estimate
- Annual rate of increase in O&M

- Estimated net square footage
- Annual rate of increase of base rent
- Annual rental increase with nine rental changes during the building's economic life

Build Variables (with Bond Financing)

- Net square feet
- Date construction starts
- Date construction ends
- Estimated land value
- Annual rate of increase in land through mid-construction
- Land purchased in a lump sum?
- Estimated construction costs
- Annual rate of increase of construction costs
- Estimated annual operating and maintenance (O&M) costs
- Annual rate of increase in O&M costs
- Construction loan interest rate
- Estimated cost of preliminary plans
- Estimated cost of working drawings
- Construction loan, preliminary plans and working drawings paid in one lump sum?
- Estimated gross square footage
- Average Coupon Yield
- Bond life in years
- Earning rate for Debt Service Reserve
- Earning rate for capitalized interest
- Earning rate for construction fund
- Underwriter's discount rate
- Underwriter's fee rate
- Insurance fee
- Other costs
- Debt Service Reserve requirement

Each of the different types of public and private financing approaches analyzed by the EFM contain this level of detail.

TECHNICAL REVIEW

Consultants find that the structure of the model (i.e., the way it uses variables to determine the cost of private and public financing methods) is appropriate for the analyses it is intended to perform. However, like all other models, results are only as good as the input assumptions used by the analyst. The input assumptions for the build option using tax-exempt financing are reviewed. Other input assumptions, such as operating and maintenance costs, construction costs and schedule, lease rates, etc., are beyond the scope of this study and are not reviewed.

Bond Financing Parameters

The EFM has a bond sizing component that provides annual debt service payments. Debt service payments, combined with the costs of operating and maintaining state buildings, determines the annual costs of owning a building. (The general process used in the EFM is similar to that discussed in a following section regarding the lease vs. build issue.)

Of the bond sizing variables reviewed, the list below indicates the ones that may need clarification when used in the EFM. Following the list, each variable is described in detail.

- Average Coupon Yield
- Earning rate for Debt Service Reserve
- Earning rate for capitalized interest
- Earning rate for construction fund
- Underwriter's discount rate
- Underwriter's fee rate
- Other costs

Average Coupon Yield

The model amortizes the net construction requirement over the bond life at the "average coupon yield" to determine annual debt service payments. This is a relatively standard approach to bond sizing. However, the definition of the term "average coupon yield" and the rate chosen for the model are not clear.

Generally speaking, a "coupon" in bond financing is the semi-annual rate of interest paid on the par (face value) amount of a bond. In most of the state's lease revenue bond issues, a bond sale contains several bonds, e.g., serial and term bonds. The 1988 Los Angeles State Building Authority Lease Revenue Bonds had 15 serial bonds and one term bond, each with its own coupon, or interest rate.

Coupons do not take into consideration the "discount" or "commission" paid to the underwriters, other costs of issuance incurred by the issuer, or discounts/premiums at which the bonds are sold to the public. Yield, on the other hand, may have several definitions. From the state or borrower's perspective, yield refers to the cost, expressed as an internal rate of return, of the capital it raises from investors in exchange for interest payments it makes to them. The cost of capital includes the underwriter discount, the state's cost of issuance, and discounts or premiums paid by the investors. This cost is often referred to as the true interest cost (TIC). What is unclear in the EFM is the rate the "average coupon yield expresses; i.e., is it a coupon rate (if so for which bond maturity) or yield? If a yield, does it include underwriter's discount in addition to the price paid by investors and the coupon rate?

The OPDM analyst using the EFM calls the State Treasurer and requests an "average coupon yield." This is probably the TIC. Since the EFM uses a single rate, the State Treasurer probably supplies the TIC, although this would have to be verified. If it is the TIC, then the model is making the debt service payments higher than they should be because it double-counts for underwriter discount, underwriter fee rate (in and of themselves a possible double counting) and other costs which may be included in the TIC. If the "average coupon yield" does not include underwriter discount and issuer's expenses, i.e., the non-arbitrage yield (see the discussion of earnings rate for the construction, capitalized interest and debt service reserve funds), then it is not double counting. The OPDM analyst needs to clarify with the State Treasurer the elements included in the "average coupon yield" and use the appropriate rate in conjunction with the underwriter discount and issuer's expense variables.

Earning Rate for Debt Service Reserve, Capitalized Interest and Construction Funds

The 1986 tax reform law requires issuers to rebate any excess income earned in the Debt Service Reserve (DSR), Capitalized Interest and Construction Funds above the publicly offered bond TIC to the federal government. For calculation purposes, the publicly offered bond TIC does not include underwriter's discount or cost of issuance.

The EFM allows the analyst to enter any earnings rate for the DSR, capitalized interest, and construction funds. The rate the analyst enters should not exceed the arbitrage yield of the bonds for these funds. If the "average coupon yield" definition includes the underwriter discount and issuers expenses, then the yield is too high. If the "average coupon yield" is the arbitrage yield, then it is correct.

Complicating the issue of the appropriate earnings rate for the debt service reserve, capitalized interest and debt service reserve funds is a change to the rebate requirements passed in the 1989 Tax Reconciliation Act. The act allows issuers to select the rebate or penalty method in regards to excess earnings. The rebate method is the same as described above. The penalty method allows the issuer to invest the gross proceeds of the issue (except the debt service reserve fund) if they are spent within two years according to the following schedule:

- a. 10 percent spent within 6 months
- b. 45 percent spent within 12 months
- c. 75 percent spent within 18 months
- d. 100 percent spent within 24 months (with a reasonable retainage of up to 5 percent until the end of 36 months to allow for contingencies)

If the proceeds are not spent according to the schedule above, the issuer must pay a penalty.

For purposes of the EFM, the arbitrage bond yield should be used for the debt-serviced reserve, capitalized interest and construction fund for those projects with construction periods exceeding two years. If the project is certain to be built within two years, then a higher earnings rate could be used. For consistency purposes, the Pooled Money Investment Board's rate is recommended. This rate is used for the cost of a construction loan (see construction variables, below) and the discount rate for comparing two alternative financing methods.

Underwriter Discount Rate, Underwriter Fee Rate and Other Costs

The underwriter discount rate often refers to the "spread" the investment banks receive for purchasing the bonds and reoffering them to the investing public. The "spread" consists of the "takedown," underwriter risk, management fee and expenses. Takedown is the "sales commission" the underwriter receives for buying the bonds and reselling them to the public. It is usually the largest component of the "spread". Underwriter risk is the fee paid to the underwriter for buying the bonds and risking the firm's capital if the underwriter resells the bonds at a loss (or if he is not able to place all the bonds with investors). The management fee is only charged in a negotiated sale and represents the charge for developing the legal and credit aspects of the bond structure. The final element of the underwriter "spread" are out-of-pocket expenses. These charges represent cost of travel, use of computers and the like for structuring the transaction. They also only accompany a

negotiated sale. In addition to these underwriting expenses, the issuer also incurs other costs such as bond counsel, printing expenses, underwriter's counsel, etc.

Whether the EFM should include these costs depends on what is contained in the "average coupon yield." If underwriter's spread and issuer's costs are already calculated in the TIC that is used as the "average coupon yield," then it is not necessary to add the Underwriter's Discount Rate, Underwriter's Fee Rate and other cost amounts to the bond sizing. If the "average coupon yield" does not include these costs, then they should be taken into consideration during bond sizing.

If underwriter discount rate, underwriter fee rate and other costs are used, then they should vary between one percent and two percent of the size of the issue. This is a general rule, as the issue size will determine the actual costs. For the five lease transactions reviewed between 1985 and 1989, the average cost was 1.74 percent of the par amount of bonds (see Table 5, below).

TABLE 5
Underwriter Discount and Issuer Costs
of Issuance for Five State of California
Lease Financing Bond Sales

	Issue	Amount	Underwriter Discount(%)	Issuer Costs(%)	Total(%)
1.	1988 LA	187,130,000	2,580,523(1.4%)	115,000 (.06%)	2,695,523 (1.44%)
2.	1985 PWBSM	104,400,000	1,944,972(1.86%)	203,206 (.19%)	2,148,178 (2.06%)
3.	1987 PWBHF	17,390,000	265,893(1.53%)	111,662 (.64%)	377,555 (2.17%)
4.	1986 PWBAP	163,090,000	2,711,000(1.66%)	845,000 (.5%)	3,556,000 (2.18%)
5.	1989 FTBR	36,870,000	351,513.84(.95%)	86,504.86 (.235%)	438,018.87 (1.188%)

1. LA = Los Angeles Building Authority
2. PWBSM = Public Works Board Southern Maximum Security Prison
3. PWBHF = Public Works Board Hi-Tech Facility, University of California
4. PWBAP = Public Works Board Amador Prison
5. FTBR = Franchise Tax Board Refunding

Relationship of the EFM to Financing Techniques Being Used to Fund Office Space Requirements

The EFM can evaluate a multitude of financing options for space requirements. These include private financing techniques such as straight leasing, lease purchase option, installment sale and public techniques including lease revenue bonds and capital outlay funding. Most of the DGS's office space needs are met by straight leasing or new construction. New construction funding was historically provided with capital outlay funds, but because of the scarcity of these funds, if new buildings are constructed they are usually funded with lease revenue bonds. The EFM model is used to determine the cost of financing new buildings with this technique. There appears to be a variation to this funding method that is not currently being evaluated in the EFM that can reduce the costs of bond financing. The variations include a reduction or elimination of capitalized interest in lease revenue bonds and initiation of a Commercial Paper Program to reduce borrowing costs during construction.

Capitalized Interest and Construction Financing

The typical office building has three basic stages that require funding; conceptual development and preliminary plans, working drawings, and construction. The EFM can accommodate different funding sources for these three stages. In the evaluation of bond financing for state office building construction, OPDM currently uses Capital Outlay monies or a loan from the Pooled Money Investment Board (PMIB) for preliminary plans and construction and pays off the construction loan with bond proceeds at the end of the construction period, i.e., capitalized interest. Another approach is to issue bonds to raise construction dollars. This requires the bond size to be increased to make interest payments during the construction period.

OPDM should include two different approaches to construction loans and capitalized interest funding to evaluate the cost of bond financing.

Construction Loan

If the DGS borrows from the PMIB it pays the interest rate the PMIB earns on its investments. To determine the construction loan interest rate, the EFM analyst uses an average PMIB rate over the previous five years. However, if DGS actually borrows from PMIB, it would have to pay the rate earned in the PMIB at the time of the borrowing. The average rate currently used in the EFM is 8.363 percent. On June 1, 1990, the PMIB rate was 8.537 percent. These are taxable interest rates and are significantly higher than short-term tax-exempt rates. On June 1, tax-exempt notes were trading at about 6.05 percent (Bond Buyer, June 4, 1990, page 1). This is 248 basis points (2.48 percent) lower than the PMIB rate. The state can substantially lower its construction loan costs by borrowing in the tax-exempt markets rather than the PMIB. This borrowing can be done with a Tax-Exempt Commercial Paper Program, described in Financing Techniques.

If the PMIB earnings were returned entirely to the state's Fund, then the additional "cost" of DGS borrowing from this fund would be cancelled by the additional "benefit" of earnings for the state's General Fund. However, the majority of the earnings in the PMIB accrue to the Local Agency Investment Fund (LAIF) whose members are municipal entities throughout the state. In the 1985-86 PMIB report over 63 percent of the PMIB earnings were returned to LAIF.

Capitalized Interest

Traditionally, bond financings for state office buildings have included capitalized interest payments during the construction period. Capitalized interest is required in lease financings because the lessee cannot begin rental payments supporting debt service until it has the beneficial use of the facility. Beneficial use does not begin until the building is occupied. Consequently, the amount of money raised in bond proceeds includes the funds necessary to make interest-only payments during construction. The increased size of the bond issue increases the annual debt service payments and cost of financing.

The EFM analyst routinely uses capitalized interest in evaluating the cost of bond financing. However, asset substitution is recommended as an alternate approach. This financing alternative eliminates the need for capitalized interest. Asset substitution is described in more detail in the section on Financing Techniques.

APPENDIX F COMPARISON OF STRAIGHT LEASE VS. LEASE PURCHASE FINANCING MODELS

INTRODUCTION

One purpose of this study is to determine whether it is cheaper to lease or build office space. A methodology to address this issue was developed after meeting with representatives from the Office of Project Development and Management (OPDM), the Office of Real Estate and Design Services (OREDS), and the Office of Asset Management. The method stresses the conceptual nature of the analysis. There was no attempt to quantify the cost of lease vs. own/build for all the office space the state currently rents and plans to rent or build in the future, as this is a major effort well beyond the scope of this study. However, an analytical approach to ascertain lease vs. build costs is provided. In the analysis, the lease approach assumes the state signs a straight lease with a developer for a renewable fixed lease term. The build approach assumes the state will issue tax-exempt bonds, either Lease Revenue Bonds or Certificates of Participation. This appendix describes the approach and results of the analysis.

The appendix is comprised of four parts. The first is a summary of the lease vs. build conceptual analyses. The second describes the methodology and the third provides additional information about the costs and benefits of leasing vs. constructing office buildings. The fourth sets forth conclusions regarding the question of whether it is cheaper to build than lease.

SUMMARY OF CONCLUSIONS

Two examples are used to compare the costs of straight leasing vs. constructing office buildings with tax-exempt lease financing: a historical and a hypothetical current analysis. The historical analysis used the Justice Department Complex built in the late 1970s to determine the cost of financing the building if the state had used lease revenue bonds for its construction (it was built with Capital Outlay Funds). Since the Justice Department Complex was built with Capital Outlay Funds, a lease is needed to compare it to the bond financing option. A lease agreement the state had with a developer to accommodate the office space needs of the Employment Development Department (EDD) was used. A further description of the historical example method and assumptions is discussed below in Methodology.

To develop the hypothetical analysis a hypothetical building was used with the same square footage as the Justice Department Complex for both the bond financing and straight leasing comparison. This approach allowed a better comparison between the costs of straight leasing vs. building over time for the same type of building. To ascertain straight lease costs, two different lease rates were compared against the bond financing example. These rates reflect leases OREDS has recently negotiated. (Details about the assumptions of the cost of the building that determined the bond size and the cost of the straight lease are discussed in the Methodology section.)

The conceptual nature of the lease vs. build question is emphasized because of the many variables and assumptions that must be included to properly address the issue. The response to the question, "Is it cheaper to lease or build?" depends on the assumptions used for these variables. The following list identifies only some of these variables.

The variables and assumptions that are necessary to determine the parameters of the lease vs. build issue are divided in three basic categories; factors that determine straight lease costs, bond financing factors and those factors common to both.

Straight Lease Factors

- How tenant improvements are incorporated into the lease
- Developer financial status
- General Sacramento area economic conditions
- General Sacramento area real estate market conditions
- Sacramento area office space supply/demand
- Sacramento vacancy rate: central, core, metro
- Length of time developer owns the land
- Escalation of base rent assumptions
- Operating and maintenance costs
- Operating and maintenance cost escalation rate
- Developer incentives (e.g., free rent for certain specific periods)

Bond Financing Factors (Build Alternative)

- State contracting procedures
- Labor requirements
- Capital Outlay Process
- State construction management procedures
- Tax-exempt bond amortization period, interest rates, costs of issuance, debt service reserve fund, capitalized interest period
- Tax-exempt market conditions
- State's lease financing credit rating

Common Factors and Assumptions

- Type of building
- Type of construction
- Construction schedule
- Quality of construction
- State-mandated requirements (e.g., handicap access)

These are some of the factors that will influence the outcome of the lease vs. build analysis. Assumptions about some of these factors, such as operating and maintenance cost escalation rates, bond interest rates, and construction costs, are described in the methodology section and reflected in the results below.

RESULTS SUMMARY

- a. In both the historical and hypothetical examples, over a 50-year building life, the cost to own a building is significantly less than straight leasing. The range of the savings, on a present value basis, for a 307,305 net square foot (NSF) building is from \$17.5 to 39.1 million. This is about \$0.35 to \$0.8 million per year or about \$1.17 to \$2.60 per net square foot per year.

- b. If the state converted its currently leased space in the Sacramento area (4,164,061 net square feet, 1988 Sacramento Facilities Plan, p. vii) into owned space the savings (on a present value basis), over a 50-year period, would range from \$4.7 to \$10.8 million per year.
- c. The cost of straight leasing is lower than the cost of lease financing for the first 15 years in the historical example and ranges from 15 to 17 in the hypothetical example.
- d. If the state were to lease rather than construct the buildings in the Department of General Services' 1989 Five Year Capital Plan, it would cost an additional \$3 to \$6.8 million per year, based on the conceptual analysis provided below.

The figures provided in the results are intended to give the reader a sense of the order of magnitude of the costs associated with the lease vs. build question based on the conceptual analysis. They provide a basis for discussion of the issue, not an answer to the question. A much more detailed review of each existing state lease and potential leases the state may enter into combined with specific cost information about new buildings is necessary to begin to answer the build vs. lease question.

METHODOLOGY

The summary above described the general approach to addressing the question "Is it cheaper to lease or build?" It also provided a list of variables and assumptions that effect the analysis. This section presents a more detailed discussion of the method, the variables used in the analysis and their definition.

The general approach was to develop annual costs for the lease vs. build options over a 50-year life of a "typical" Sacramento area building. The annual costs were evaluated at three points in time; the entire 50-year period, the first five years of occupancy and the point at which the cost of leasing equaled the cost of building using tax-exempt bond financing (the break-even point). The present value of the difference for the build option was compared, using lease revenue bond financing, minus the straight lease options. A negative result means that it is cheaper to build within the given time period. A positive result indicates that it is less costly to enter into a straight lease for the specific time period. The break-even point reflects the number of years it takes for the cost of straight leasing to equal the cost of building, on a present value basis. The attached schedules illustrate the results of the analysis. The variables used in the analysis are defined before discussing the results.

STRAIGHT LEASE VARIABLES

- Total net square footage leased
- Cost per net square foot
- Initial base rent cost
- Base rental portion of total rent
- Operating and maintenance portion of total rent
- Base rent inflation rate
- Operating and maintenance inflation rate

Total Net Square Footage Leased, Cost Per Net Square Foot and Initial Lease Base Rent Cost

The initial lease base rent is the annual rent the state agrees to pay upon signing a straight lease agreement. In the historical example, the state signed a 15 year firm lease term with a developer for 42,405 useable square feet (net square feet) for \$29,259 per month or \$351,108 per year for office space required by the Employment Development Department. This is equivalent to 69 cents per square foot per month. Since the analysis compares this lease with the net square foot equivalent of the Justice Department Complex, an annual cost of leasing an equivalent Justice Department building is derived by multiplying the 69 cents (cost per square foot) times the square footage of the Justice Department Complex (307,305 NSF, the total NSF leased) times 12 (months). The result is \$2,544,485 ($\$0.69 \times 307,305 \times 12 = \$2,544,485$) shown under the lease assumption column in Schedule I.

In the hypothetical analysis, OREDS was asked for a lease the state had recently entered into for a building similar to the Justice Department Building. This request was in some ways more difficult to comply with than the historical example. In today's Sacramento market there appears to be a sufficient supply of office space, forcing some developers to offer free rent for a short period of time (less than a year). However, the free rent is available for certain types of buildings that do not necessarily conform to the specifications of the Justice Department Building. Another factor complicating the analysis is building location. In selecting the Justice Department Complex, an attempt was made to use a "typical" office building that is representative of the Sacramento area lease rental market (and construction market for the build scenario). However, this building is not necessarily representative of buildings the state leases in areas outside of Sacramento. Lease rates are much higher in Los Angeles and the San Francisco Bay area. They are lower in Fresno, Redding and other smaller metropolitan communities. Some of these factors are annotated to stress the fact that the results of the "quantitative" evaluation are conceptual in nature and are not to be construed as representing actual costs. A more detailed study of lease and building costs of each proposed state building would have to be done to answer the specific question of whether it is cheaper for the state to rent or own its office buildings.

It was found that a single lease rate for the Sacramento area would not be representative of the wide range of leasing costs and therefore two rates were selected: \$1.15 and \$1.35 per square foot per month. These rates are within the general limits the state is currently negotiating for office space.

Base Rental and Operating and Maintenance Rate Portions of Total Rent Payments and Base Rental Inflation Rate

Lease rental payments consist of two components; the base rental rate and the operating and maintenance rate. OREDS uses the Building Office Managers Association percentage of total rent for California office space, about 39 percent, as the portion of the total rent that is assigned to operating and maintenance costs to negotiate its operating and maintenance escalation rate. The remaining 61 percent is the base rent.

The rental increase rate per year for the base rent depends on the terms and conditions of the lease. In most cases the lease has a fixed term agreement, for example five years, where the base rent remains the same for the duration of the lease. After five years the terms of the lease are renegotiated and the base rent is increased in most cases.

Schedules I and II show how the base rental is estimated and how the annual rental increase is calculated. The total rent payment was divided into base rent and operating and

maintenance costs according to the OREDS convention of 61 percent and 39 percent respectively. For the base rent the term of the lease was assumed to be five years and at the end of each five-year period the base rent was escalated at five percent (the escalation rate currently being used in OPDM's Economic Forecasting Model). This provided the escalated base rent portion for the next five year lease term. This approach can be applied to both the historical and hypothetical examples.

Operating and Maintenance Annual Inflation Rate

The 39 percent of total rent is escalated annually at five percent to reflect operating and maintenance cost inflation. The five percent figure is the same rate OPDM uses in its Economic Forecasting Model.

BOND FINANCING VARIABLES

- Construction Cost
- Construction Expenditure Schedule
- Operating and Maintenance Costs
- Operating and Maintenance Inflation Rate
- Bond Financing Parameters; amortization period, interest rates, costs of issuance (including underwriter discount), debt service reserve, capitalized interest period

Construction Cost and Construction Expenditure Schedule

In the Justice Department Complex example, OPDM provided the actual cost of the land, planning, working drawings and construction for the buildings: \$32,919,500. In addition to total cost, the expenditure schedule of the Capital Outlay Funds was needed for bond sizing purposes. However, this was not readily available from OPDM. OPDM did provide the summary of expenditures, by fiscal year, which was used in the analysis.

For the hypothetical building cost, the cost of building construction in the Sacramento area for a "typical" state building was discussed with the consulting team's architect and an estimator in the Department of General Services. They independently provided a figure of \$115 per square foot for construction only (excluding land, planning, working drawings and construction management costs). As a conservative measure, 20 percent of the construction cost was added for planning, design and construction management, increasing the total cost to \$138 per square foot. To derive land costs it was assumed that the land cost was in the same proportion to construction as the Justice Department Building, i.e., 8.5 percent. It was also assumed that the expenditure schedule for the hypothetical building would be in the same annual percentages as the Justice Department Building; approximately 10.8 percent, 18.2 percent and 71 percent in years one through three.

Operating and Maintenance Costs and Inflation Rate

Operating and maintenance costs are charged to the executive departments occupying state-owned buildings through the Building Rental Account. The Department of General Services establishes an operating and maintenance cost and bills each department based on the useable square feet the department occupies. In fiscal year 1989-90, the cost of maintaining the state's buildings was approximately \$4.76/year, on a gross square foot basis. Consultants converted this figure to a net square foot basis by dividing by 1.25 to

arrive at the annual operating and maintenance cost in the hypothetical example, \$3.81, and escalated at five percent per year.

In the historical building analysis, Consultants did not have information about the state's 1978 operating and maintenance costs. Consequently, the \$3.81 was deflated at five percent per year to the first year of the lease, 1978, to derive the operating and maintenance costs in this example. This rate was then escalated at five percent per year, lower than the general inflation rate in the early 1980s, but consistent with inflation since 1983 and for the remaining 45 years of the analysis.

Bond Financing Parameters

a. Amortization Period

The amortization period is the time it takes to pay the principal on the bonds and is often referred to as the bond term. The longer the amortization period the more interest the issuer pays throughout the term of the bonds, but the lower the annual debt service payments. The amortization period chosen to size the bonds for the build alternative was twenty years. Five official statements from previous lease financings, which had an average amortization for the final bond maturity of about seventeen years, were reviewed. Consistent with the conservative stance of the analysis (i.e., increase the cost of the bond financing alternative), twenty years was chosen as the final maturity for the bonds. The amortization structure is shown on Schedule III, Debt Service Schedule for both the Justice Department Complex and the hypothetical office construction examples.

b. Interest Rates

For the Justice Department Complex, the intent was to recreate the cost of tax-exempt financing for these buildings; therefore, historical interest rates are used. The lease agreement for EDD began in 1978, which would be the beginning of base rental payments in the bond financing scenario. However, a three year capitalized interest period was included, which is the time it takes to build the building in the bond financing options. This is a conservative assumption in that capitalized interest increases the bond size and debt service payments. One method by which the state can avoid capitalized interest costs in its future bond financings is using "asset substitution." Asset substitution is discussed in the financing techniques section.

To compare the financing option to the straight lease, rental payments cannot begin until the lessee has beneficial use of the facility. Therefore, the beginning of the Lease Purchase Payments, as shown on Schedule I, starts in 1978, but the sale of the bonds would have been three years earlier to account for the capitalized interest period. The amortization period appears to be only seventeen years in Schedule I, but is actually twenty if you take into consideration the three-year capitalized interest period.

The bonds should have been sold in 1975. However, maintaining the conservative approach, 1978 interest rates were used as they were generally higher than 1975 rates. There was also a need to be consistent with the time of signing of the 1978 EDD lease. The next assumption was to choose the specific date of issuance, since interest rates change on a daily basis. It was assumed that the bonds were sold on June 1 and used the rates for a AA bond sold on that date for ten-year serial bond

maturities and the twenty-year term bond maturity (see Schedule II). The Delphis Hanover Index was used. It is a national service that provides interest rates for bonds with credit ratings ranging from AAA to BBB+. The AA rating was the implied state's rating for lease-supported debt. Following general credit rating convention, the rating on lease revenue bonds is usually one step lower than an entity's general obligation rating, which, in this case was AAA in 1978. The scale of interest rates is shown in the bond sizing on Schedule III, titled Debt Service Schedule. The rates run from 4.8 percent for a four-year serial bond to 5.95 percent for the twenty-year term bond.

The interest rates for the hypothetical example were not as difficult to choose. Again, the Delphis Hanover Index was used for a AA credit for a bond issued today. The state currently has a AAA rating and its lease revenue bonds would be most likely rated AA, depending on the other legal and credit characteristics of a specific lease financing. These interest rates are shown on Schedule III, titled Hypothetical Office Construction Debt Service Schedule.

c. Costs of Issuance

Costs of issuance include underwriter's discount (their "commission" in selling the bonds) and issuer's expenses, such as bond counsel, trustee, appraisal reports, printing, etc. To determine these costs, five official statements were reviewed from previous state lease revenue bond issues between 1985 and 1989 provided by the State Treasurer and underwriters. The average cost for these five issues was 1.74 percent of the par amount (face value) of bonds and was the percentage used in the analysis.

d. Debt Service Reserve

To determine the deposit to the Debt Service Reserve Fund, the five official statements were used again. The range of debt service reserve requirements was 0 percent, 50 percent, and 100 percent of the maximum annual debt service. The credit, details of the legal structure and general market conditions for a specific transaction would determine the debt service reserve requirements. For our hypothetical example we used a 50 percent requirement as it is consistent with the documents reviewed and is currently being used in OPDM's Economic Forecasting Model.

e. Capitalized Interest Period

The capitalized interest period reflects the construction period for the building and a period of reserve to allow for unanticipated delays in the project which would prevent the lessee from occupying the facility and beginning its base rental payments. The construction period for the Justice Department Complex was two years, with an additional year for planning. Maintaining the conservative approach, a three-year capitalized interest period was used; about a 2.5 year working drawing and construction period and 0.5 year contingency period.

State of California

Auditor General

Justice Department Complex Analysis, Schedule I (page 1 of 3)

Lease Assumptions:		Construction Cost:		Building Assumptions:		Present Value Difference:	
Total Annual Cost	\$2,544,485	Land Acquisition	\$2,600,000	Gross Sq. Ft.	377,325	(purchase – lease)	
Net Sq. Ft.(1)	307,305	Construction	\$30,319,500	Net Sq. Ft.	307,305	After 5 Yrs.	\$7,430,151
Cost/NSF/Yr.(1)	\$8.28			O&M Cost/Yr.	\$684,561	Break Even Point	Year 24
Rental Increase/Yr.	5.00%	Total Cost	\$32,919,500	O&M Cost/NSF/Yr.	\$2.23	After 50 Yrs.	(\$30,796,501)
O&M portion	992,349			O&M Inflation	5.00%		
Rent Portion	1,552,136					Discount Rate	5.8856668%

	Annual Straight		Lease Purchase		O&M	Total Annual	Annual Payment
	Year	Lease Payments	Payments	Payments	Payments	Payment (1)	Difference
0	1978	2,544,485	3,549,477.50	684,561		4,234,039	1,689,553
1	1979	2,594,103	3,550,837.50	718,789		4,269,627	1,675,524
2	1980	2,646,201	3,552,337.50	754,729		4,307,066	1,660,865
3	1981	2,700,904	3,553,587.50	792,465		4,346,053	1,645,148
4	1982	2,758,343	3,549,182.50	832,088		4,381,271	1,622,928
5	1983	3,247,480	3,553,962.50	873,693		4,427,655	1,180,176
6	1984	3,310,806	3,552,887.50	917,378		4,470,265	1,159,459
7	1985	3,377,298	3,550,862.50	963,246		4,514,109	1,136,811
8	1986	3,447,115	3,551,512.50	1,011,409		4,562,921	1,115,807
9	1987	3,520,422	3,554,087.50	1,061,979		4,616,067	1,095,645
10	1988	4,144,699	3,553,935.00	1,115,078		4,669,013	524,315
11	1989	4,225,520	3,550,655.00	1,170,832		4,721,487	495,967
12	1990	4,310,383	3,551,310.00	1,229,374		4,780,684	470,301
13	1991	4,399,489	3,553,040.00	1,290,842		4,843,882	444,394
14	1992	4,493,050	3,550,250.00	1,355,384		4,905,634	412,585
15	1993	5,289,802	3,552,642.50	1,423,154		4,975,796	(314,006)
16	1994	5,392,954	3,549,325.00	1,494,311		5,043,636	(349,317)
17	1995	5,501,262	0.00	1,569,027		1,569,027	(3,932,235)
18	1996	5,614,986	0.00	1,647,478		1,647,478	(3,967,508)
19	1997	5,734,397	0.00	1,729,852		1,729,852	(4,004,545)
20	1998	6,751,277	0.00	1,816,345		1,816,345	(4,934,932)
21	1999	6,882,927	0.00	1,907,162		1,907,162	(4,975,765)
22	2000	7,021,160	0.00	2,002,520		2,002,520	(5,018,639)
23	2001	7,166,304	0.00	2,102,646		2,102,646	(5,063,657)
24	2002	7,318,705	0.00	2,207,778		2,207,778	(5,110,926)
25	2003	8,616,531	0.00	2,318,167		2,318,167	(6,298,363)
26	2004	8,784,553	0.00	2,434,076		2,434,076	(6,350,477)

State of California

Auditor General

Justice Department Complex Analysis, Schedule I (page 2 of 3)

Lease Assumptions:		Construction Cost:		Building Assumptions:		Present Value Difference:	
Total Annual Cost	\$2,544,485	Land Acquisition	\$2,600,000	Gross Sq.Ft.	377,325	(purchase – lease)	
Net Sq. Ft.(1)	307,305	Construction	\$30,319,500	Net Sq.Ft.	307,305	After 5 Yrs.	\$7,430,151
Cost/NSF/Yr.(1)	\$8.28	Total Cost	\$32,919,500	O&M Cost/Yr.	\$684,561	Break Even Point	Year 24
Rental Increase/Yr.	5.00%			O&M Cost/NSF/Yr.	\$2.23	After 50 Yrs.	(\$30,796,501)
O&M portion	992,349			O&M Inflation	5.00%		
Rent Portion	1,552,136	Discount Rate 5.8856668%					

	Annual Straight		Lease Purchase		O&M		Total Annual		Annual Payment	
	Year	Lease Payments	Payments	Payments	Payments	Payment (1)	Payment	Difference		
27	2005	8,960,977	0.00	2,555,780	2,555,780	2,555,780		(6,405,197)		
28	2006	9,146,221	0.00	2,683,569	2,683,569	2,683,569		(6,462,653)		
29	2007	9,340,728	0.00	2,817,747	2,817,747	2,817,747		(6,522,981)		
30	2008	10,997,119	0.00	2,958,634	2,958,634	2,958,634		(8,038,485)		
31	2009	11,211,563	0.00	3,106,566	3,106,566	3,106,566		(8,104,997)		
32	2010	11,436,729	0.00	3,261,894	3,261,894	3,261,894		(8,174,835)		
33	2011	11,673,153	0.00	3,424,989	3,424,989	3,424,989		(8,248,164)		
34	2012	11,921,399	0.00	3,596,238	3,596,238	3,596,238		(8,325,161)		
35	2013	14,035,421	0.00	3,776,050	3,776,050	3,776,050		(10,259,370)		
36	2014	14,309,111	0.00	3,964,853	3,964,853	3,964,853		(10,344,258)		
37	2015	14,596,487	0.00	4,163,096	4,163,096	4,163,096		(10,433,391)		
38	2016	14,898,231	0.00	4,371,250	4,371,250	4,371,250		(10,526,980)		
39	2017	15,215,062	0.00	4,589,813	4,589,813	4,589,813		(10,625,249)		
40	2018	17,913,148	0.00	4,819,303	4,819,303	4,819,303		(13,093,845)		
41	2019	18,262,455	0.00	5,060,269	5,060,269	5,060,269		(13,202,186)		
42	2020	18,629,227	0.00	5,313,282	5,313,282	5,313,282		(13,315,945)		
43	2021	19,014,337	0.00	5,578,946	5,578,946	5,578,946		(13,435,391)		
44	2022	19,418,703	0.00	5,857,893	5,857,893	5,857,893		(13,560,809)		
45	2023	22,862,221	0.00	6,150,788	6,150,788	6,150,788		(16,711,433)		
46	2024	23,308,034	0.00	6,458,328	6,458,328	6,458,328		(16,849,707)		
47	2025	23,776,138	0.00	6,781,244	6,781,244	6,781,244		(16,994,894)		
48	2026	24,267,648	0.00	7,120,306	7,120,306	7,120,306		(17,147,341)		
49	2027	24,783,732	0.00	7,476,321	7,476,321	7,476,321		(17,307,411)		
Total		\$501,772,998	Total	\$60,379,893	\$143,311,526	\$203,691,418		(\$298,081,580)		

(1) The Cost per NSF is taken from the 1978 lease for the EDD building
the square footage was increased to equal that of the Justice Building.

(1) The Cost per NSF is taken from the 1978 lease for the EDD building the square footage was increased to equal that of the Justice Building.

State of California

Auditor General

Justice Department Complex Analysis

Lease Increase Calculations, Schedule I (page 3 of 3)

O&M portion	992,349
Rent Portion	1,552,136
Rent Inflation	5.00%
O&M Inflation	5.00%

5 year Period	5 year O&M Base (1)	5 year Rent Base (2)	5 year Total Base Rents (1)+(2)
1978 - 82	992,349	1,552,136	2,544,485
1983 - 87	1,266,517	1,980,963	3,247,480
1988 - 92	1,616,432	2,528,266	4,144,699
1993 - 97	2,063,023	3,226,779	5,289,802
1998 - 02	2,632,998	4,118,279	6,751,277
2003 - 07	3,360,447	5,256,084	8,616,531
2008 - 12	4,288,877	6,708,243	10,997,119
2013 - 17	5,473,814	8,561,607	14,035,421
2018 - 22	6,986,128	10,927,021	17,913,148
2023 - 27	8,916,266	13,945,955	22,862,221

State of California

Auditor General

Hypothetical Office Analysis, Schedule II - A, assuming \$1.15/month (page 1 of 3)

Hypothetical Office Analysis, Schedule II - A, assuming \$1.00 per sq. ft. of office space									
Lease Assumptions:		Construction Cost:		Building Assumptions:		Present Value Difference:			
Total Annual Cost	\$4,240,809	Land Acquisition	\$4,426,022	Gross Sq. Ft.	337,325	(purchase - Lease)			
Net Sq. Ft.	307,305	Construction	\$52,070,850	Net Sq. Ft.	307,305	After 5 Yrs.			\$16,457,610
Cost/NSF/Yr.	\$13.80			O&M Cost/Yr.	\$1,170,832	Break Even Point			Year 34
Rental Increase/Y	5.00%	Total Cost	\$56,496,872	O&M Cost/NSF/Yr.	\$3.81	After 50 Yrs.			(\$17,510,394)
O&M portion	1,653,916			O&M Inflation	5.00%				
Rent Portion	2,586,893					Discount Rate			7.2724010%
		Annual Straight		Lease Purchase		O&M	Total Annual	Annual Payment	
	Year	Lease Payments		Payments		Payments	Payment (1)	Difference	
0	1991	4,240,809		6,887,325.00		1,170,832	8,058,157	3,817,348	
1	1992	4,323,505		6,885,102.50		1,229,374	8,114,476	3,790,971	
2	1993	4,410,335		6,886,505.00		1,290,842	8,177,347	3,767,012	
3	1994	4,501,507		6,885,255.00		1,355,384	8,240,639	3,739,132	
4	1995	4,597,238		6,886,700.00		1,423,154	8,309,854	3,712,616	
5	1996	5,412,466		6,884,662.50		1,494,311	8,378,974	2,966,508	
6	1997	5,518,009		6,883,282.50		1,569,027	8,452,309	2,934,300	
7	1998	5,628,830		6,886,342.50		1,647,478	8,533,821	2,904,991	
8	1999	5,745,191		6,887,257.50		1,729,852	8,617,110	2,871,919	
9	2000	5,867,370		6,884,760.00		1,816,345	8,701,105	2,833,735	
10	2001	6,907,831		6,887,560.00		1,907,162	8,794,722	1,886,891	
11	2002	7,042,534		6,883,640.00		2,002,520	8,886,160	1,843,626	
12	2003	7,183,972		6,887,120.00		2,102,646	8,989,766	1,805,795	
13	2004	7,332,481		6,886,840.00		2,207,778	9,094,618	1,762,137	
14	2005	7,488,416		6,886,360.00		2,318,167	9,204,527	1,716,111	
15	2006	8,816,337		6,883,880.00		2,434,076	9,317,956	501,618	
16	2007	8,988,256		6,887,600.00		2,555,780	9,443,380	455,124	
17	2008	9,168,770		0.00		2,683,569	2,683,569	(6,485,202)	
18	2009	9,358,311		0.00		2,817,747	2,817,747	(6,540,564)	
19	2010	9,557,328		0.00		2,958,634	2,958,634	(6,598,694)	
20	2011	11,252,129		0.00		3,106,566	3,106,566	(8,145,563)	
21	2012	11,471,545		0.00		3,261,894	3,261,894	(8,209,651)	
22	2013	11,701,933		0.00		3,424,989	3,424,989	(8,276,944)	
23	2014	11,943,839		0.00		3,596,238	3,596,238	(8,347,601)	
24	2015	12,197,841		0.00		3,776,050	3,776,050	(8,421,791)	
25	2016	14,360,885		0.00		3,964,853	3,964,853	(10,396,032)	
26	2017	14,640,922		0.00		4,163,096	4,163,096	(10,477,826)	

State of California

Auditor General

Hypothetical Office Analysis, Schedule II-A, assuming \$1.15/month (page 2 of 3)

Lease Assumptions:		Construction Cost:		Building Assumptions:		Present Value Difference:	
Total Annual Cost	\$4,240,809	Land Acquisition	\$4,426,022	Gross Sq. Ft.	337,325	(purchase - Lease)	
Net Sq. Ft.	307,305	Construction	\$52,070,850	Net Sq. Ft.	307,305	After 5 Yrs.	\$16,457,610
Cost/NSF/Yr.	\$13.80	Total Cost	\$56,496,872	O&M Cost/Yr.	\$1,170,832	Break Even Point	Year 34
Rental Increase/Y	5.00%			O&M Cost/NSF/Yr.	\$3.81	After 50 Yrs.	(\$17,510,394)
O&M portion	1,653,916			O&M Inflation	5.00%		
Rent Portion	2,586,893					Discount Rate	7.2724010%
	Year	Annual Straight		Lease Purchase		Total Annual	
		Lease Payments		Payments		Payment (1)	Difference
27	2018	14,934,961		0.00		4,371,250	(10,563,711)
28	2019	15,243,702		0.00		4,589,813	(10,653,889)
29	2020	15,567,880		0.00		4,819,303	(10,748,577)
30	2021	18,328,532		0.00		5,060,269	(13,268,263)
31	2022	18,685,938		0.00		5,313,282	(13,372,656)
32	2023	19,061,215		0.00		5,578,946	(13,482,269)
33	2024	19,455,256		0.00		5,857,893	(13,597,362)
34	2025	19,868,998		0.00		6,150,788	(13,718,210)
35	2026	23,392,368		0.00		6,458,328	(16,934,040)
36	2027	23,848,519		0.00		6,781,244	(17,067,275)
37	2028	24,327,478		0.00		7,120,306	(17,207,171)
38	2029	24,830,384		0.00		7,476,321	(17,354,063)
39	2030	25,358,436		0.00		7,850,138	(17,508,299)
40	2031	29,855,247		0.00		8,242,644	(21,612,603)
41	2032	30,437,425		0.00		8,654,777	(21,782,648)
42	2033	31,048,711		0.00		9,087,515	(21,961,196)
43	2034	31,690,562		0.00		9,541,891	(22,148,670)
44	2035	32,364,505		0.00		10,018,986	(22,345,519)
45	2036	38,103,702		0.00		10,519,935	(27,583,767)
46	2037	38,846,724		0.00		6,458,328	(32,388,397)
47	2038	39,626,897		0.00		11,598,228	(28,028,669)
48	2039	40,446,079		0.00		12,178,140	(28,267,939)
49	2040	41,306,220		0.00		12,787,047	(28,519,174)
Total		\$836,288,331	Total	\$117,060,193	\$240,523,739	\$357,583,931	(\$478,704,400)

State of California

Auditor General

Hypothetical Office Analysis

Lease Increase Calculations, Schedule II - A, assuming \$1.15/month (page 3 of 3)

O&M portion	1,653,916
Rent Portion	2,586,893
Rent Inflation	5.00%
O&M Inflation	5.00%

5 year Period	5 year O&M Base (1)	5 year Rent Base (2)	5 year Total Base Rents (1)+(2)
1991 - 95	1,653,916	2,586,893	4,240,809
1996 - 00	2,110,862	3,301,604	5,412,466
2001 - 04	2,694,054	4,213,777	6,907,831
2005 - 09	3,438,372	5,377,966	8,816,337
2010 - 14	4,388,330	6,863,799	11,252,129
2015 - 19	5,600,745	8,760,140	14,360,885
2020 - 24	7,148,128	11,180,405	18,328,532
2025 - 29	9,123,023	14,269,344	23,392,368
2030 - 34	11,643,547	18,211,701	29,855,247
2035 - 39	14,860,444	23,243,258	38,103,702

State of California

Auditor General

Hypothetical Office Analysis, Schedule II-B, assuming \$1.35/month (page 1 of 3)

Lease Assumptions:		Construction Cost:		Building Assumptions:		Present Value Difference:	
Total Annual Cost	\$4,978,341	Land Acquisition	\$4,426,022	Gross Sq.Ft.	337,325	(purchase - Lease)	
Net Sq. Ft.	307,305	Construction	\$52,070,850	Net Sq.Ft.	307,305	After 5 Yrs.	\$13,114,619
Cost/NSF/Yr.	\$16.20	Total Cost	\$56,496,872	O&M Cost/Yr.	\$1,170,832	Break Even Point	Year 25
Rental Increase/Yr	5.00%			O&M Cost/NSF/Yr.	\$3.81	After 50 Yrs.	(\$39,150,106)
O&M portion	1,941,553			O&M Inflation	5.00%	Discount Rate	7.274010%
Rent Portion	3,036,788						
Annual Straight		Lease Purchase		O&M		Annual Payment	
Year	Lease Payments	Payments	Payments	Payments	Total Annual Payment (1)	Difference	
0	4,978,341	6,887,325.00	1,170,832	8,058,157	3,079,816		
1	5,075,419	6,885,102.50	1,229,374	8,114,476	3,039,058		
2	5,177,350	6,886,505.00	1,290,842	8,177,347	2,999,997		
3	5,284,378	6,885,255.00	1,355,384	8,240,639	2,956,261		
4	5,396,758	6,886,700.00	1,423,154	8,309,854	2,913,096		
5	6,353,765	6,884,662.50	1,494,311	8,378,974	2,025,209		
6	6,477,663	6,883,282.50	1,569,027	8,452,309	1,974,646		
7	6,607,757	6,886,342.50	1,647,478	8,533,821	1,926,064		
8	6,744,355	6,887,257.50	1,729,852	8,617,110	1,872,755		
9	6,887,782	6,884,760.00	1,816,345	8,701,105	1,813,322		
10	8,109,193	6,887,560.00	1,907,162	8,794,722	685,529		
11	8,267,322	6,883,640.00	2,002,520	8,886,160	618,838		
12	8,433,358	6,887,120.00	2,102,646	8,989,766	556,408		
13	8,607,695	6,886,840.00	2,207,778	9,094,618	486,923		
14	8,790,750	6,886,360.00	2,318,167	9,204,527	413,778		
15	10,349,613	6,883,880.00	2,434,076	9,317,956	(1,031,658)		
16	10,551,431	6,887,600.00	2,555,780	9,443,380	(1,108,051)		
17	10,763,339	0.00	2,683,569	2,683,569	(8,079,771)		
18	10,985,843	0.00	2,817,747	2,817,747	(8,168,096)		
19	11,219,472	0.00	2,958,634	2,958,634	(8,260,838)		
20	13,209,021	0.00	3,106,566	3,106,566	(10,102,455)		
21	13,466,597	0.00	3,261,894	3,261,894	(10,204,702)		
22	13,737,051	0.00	3,424,989	3,424,989	(10,312,062)		
23	14,021,029	0.00	3,596,238	3,596,238	(10,424,790)		
24	14,319,205	0.00	3,776,050	3,776,050	(10,543,155)		
25	16,858,430	0.00	3,964,853	3,964,853	(12,893,577)		
26	17,187,169	0.00	4,163,096	4,163,096	(13,024,073)		

State of California

Auditor General

Hypothetical Office Analysis, Schedule II -B, assuming \$1.35/month (page 2 of 3)

Hypothetical Office Analysis, Schedule II B, assuming \$1.00/month sq ft									
Lease Assumptions:		Construction Cost:		Building Assumptions:		Present Value Difference:			
Total Annual Cost	\$4,978,341	Land Acquisition	\$4,426,022	Gross Sq.Ft.	337,325	(purchase – Lease)			
Net Sq. Ft.	307,305	Construction	\$52,070,850	Net Sq.Ft.	307,305	After 5 Yrs.			\$13,114,619
Cost/NSF/Yr.	\$16.20			O&M Cost/Yr.	\$1,170,832	Break Even Point			Year 25
Rental Increase/Y	5.00%	Total Cost	\$56,496,872	O&M Cost/NSF/Yr.	\$3.81	After 50 Yrs.			(\$39,150,106)
O&M portion	1,941,553			O&M Inflation	5.00%				
Rent Portion	3,036,788					Discount Rate			7.2724010%
	Year	Annual Straight		Lease Purchase		O&M	Total Annual	Annual Payment	
		Lease Payments		Payments		Payments	Payment (1)	Difference	
27	2018	17,532,345		0.00		4,371,250	4,371,250	(13,161,095)	
28	2019	17,894,781		0.00		4,589,813	4,589,813	(13,304,968)	
29	2020	18,275,337		0.00		4,819,303	4,819,303	(13,456,034)	
30	2021	21,516,103		0.00		5,060,269	5,060,269	(16,455,834)	
31	2022	21,935,667		0.00		5,313,282	5,313,282	(16,622,385)	
32	2023	22,376,209		0.00		5,578,946	5,578,946	(16,797,263)	
33	2024	22,838,778		0.00		5,857,893	5,857,893	(16,980,885)	
34	2025	23,324,476		0.00		6,150,788	6,150,788	(17,173,688)	
35	2026	27,460,605		0.00		6,458,328	6,458,328	(21,002,278)	
36	2027	27,996,087		0.00		6,781,244	6,781,244	(21,214,843)	
37	2028	28,558,343		0.00		7,120,306	7,120,306	(21,438,037)	
38	2029	29,148,712		0.00		7,476,321	7,476,321	(21,672,390)	
39	2030	29,768,599		0.00		7,850,138	7,850,138	(21,918,461)	
40	2031	35,047,464		0.00		8,242,644	8,242,644	(26,804,820)	
41	2032	35,730,890		0.00		8,654,777	8,654,777	(27,076,113)	
42	2033	36,448,487		0.00		9,087,515	9,087,515	(27,360,971)	
43	2034	37,201,964		0.00		9,541,891	9,541,891	(27,660,072)	
44	2035	37,993,114		0.00		10,018,986	10,018,986	(27,974,128)	
45	2036	44,730,433		0.00		10,519,935	10,519,935	(34,210,498)	
46	2037	45,602,676		0.00		6,458,328	6,458,328	(39,144,349)	
47	2038	46,518,532		0.00		11,598,228	11,598,228	(34,920,303)	
48	2039	47,480,180		0.00		12,178,140	12,178,140	(35,302,040)	
49	2040	48,489,911		0.00		12,787,047	12,787,047	(35,702,864)	
	Total	\$981,729,780		\$117,060,193		\$240,523,739	\$357,583,931	(\$624,145,848)	

State of California

Auditor General

Hypothetical Office Analysis

Lease Increase Calculations, Schedule II-B, assuming \$1.35/month (page 3 of 3)

O&M portion	1,941,553
Rent Portion	3,036,788
Rent Inflation	5.00%
O&M Inflation	5.00%

5 year Period	5 year O&M Base (1)	5 year Rent Base (2)	5 year Total Base Rents (1)+(2)
1991 - 95	1,941,553	3,036,788	4,978,341
1996 - 00	2,477,968	3,875,797	6,353,765
2001 - 04	3,162,585	4,946,608	8,109,193
2005 - 09	4,036,349	6,313,264	10,349,613
2010 - 14	5,151,518	8,057,503	13,209,021
2015 - 19	6,574,788	10,283,642	16,858,430
2020 - 24	8,391,280	13,124,823	21,516,103
2025 - 29	10,709,636	16,750,969	27,460,605
2030 - 34	13,668,511	21,378,953	35,047,464
2035 - 39	17,444,869	27,285,564	44,730,433

SCHEDULE III
(Part 1)

Justice Department Complex 37,935,000 Lease Revenue Bonds Series 1978 DEBT SERVICE SCHEDULE				
DATE	PRINCIPAL	COUPON	INTEREST	DEBT SERVICE
6/01/1978	-	-	-	-
6/01/1979	-	-	2,119,477.50	2,119,477.50
6/01/1980	-	-	2,119,477.50	2,119,477.50
6/01/1981	-	-	2,119,477.50	2,119,477.50
6/01/1982	1,430,000.00	4.800%	2,119,477.50	3,549,477.50
6/01/1983	1,500,000.00	4.900%	2,050,837.50	3,550,837.50
6/01/1984	1,575,000.00	5.000%	1,977,337.50	3,552,337.50
6/01/1985	1,655,000.00	5.100%	1,898,587.50	3,553,587.50
6/01/1986	1,735,000.00	5.200%	1,814,182.50	3,549,182.50
6/01/1987	1,830,000.00	5.250%	1,723,962.50	3,553,962.50
6/01/1988	1,925,000.00	5.300%	1,627,887.50	3,552,887.50
6/01/1989	2,025,000.00	5.400%	1,525,862.50	3,550,862.50
6/01/1990	2,135,000.00	5.500%	1,416,512.50	3,551,512.50
6/01/1991	2,255,000.00	5.550%	1,299,087.50	3,554,087.50
6/01/1992	2,380,000.00	5.600%	1,173,935.00	3,553,935.00
6/01/1993	2,510,000.00	5.950%	1,040,655.00	3,550,655.00
6/01/1994	2,660,000.00	5.950%	891,310.00	3,551,310.00
6/01/1995	2,820,000.00	5.950%	733,040.00	3,553,040.00
6/01/1996	2,985,000.00	5.950%	565,250.00	3,550,250.00
6/01/1997	3,165,000.00	5.950%	387,642.50	3,552,642.50
6/01/1998	3,350,000.00	5.950%	199,325.00	3,549,325.00
TOTAL	37,935,000.00	-	28,803,325.00	66,738,325.00

YIELD STATISTICS

Accrued Interest from 06/01/1978 to 06/01/1978...	-
Average Life.....	13.270 YEARS
Bond Years.....	\$503,400.00
Average Coupon.....	5.7217571%
Net Interest Cost (NIC).....	5.8528792%
Bond Yield for Arbitrage Purposes.....	5.6889850%
True Interest Cost (TIC).....	5.8856668%
Effective Interest Cost (EIC).....	5.8856668%

SCHEDULE III
(Part 2)

Hypothetical Office Construction \$66,825,000 Lease Revenue Bonds Series 1991 DEBT SERVICE SCHEDULE				
DATE	PRINCIPAL	COUPON	INTEREST	DEBT SERVICE
6/01/1991	-	-	-	-
6/01/1992	-	-	4,682,325.00	4,682,325.00
6/01/1993	-	-	4,682,325.00	4,682,325.00
6/01/1994	-	-	4,682,325.00	4,682,325.00
6/01/1995	2,205,000.00	6.450%	4,682,325.00	6,887,325.00
6/01/1996	2,345,000.00	6.550%	4,540,102.50	6,885,102.50
6/01/1997	2,500,000.00	6.650%	4,386,505.00	6,886,505.00
6/01/1998	2,665,000.00	6.700%	4,220,255.00	6,885,255.00
6/01/1999	2,845,000.00	6.750%	4,041,700.00	6,886,700.00
6/01/2000	3,035,000.00	6.800%	3,849,662.50	6,884,662.50
6/01/2001	3,240,000.00	6.850%	3,643,282.50	6,883,282.50
6/01/2002	3,465,000.00	6.900%	3,421,342.50	6,886,342.50
6/01/2003	3,705,000.00	6.950%	3,182,257.50	6,887,257.50
6/01/2004	3,960,000.00	7.000%	2,924,760.00	6,884,760.00
6/01/2005	4,240,000.00	7.050%	2,647,560.00	6,887,560.00
6/01/2006	4,535,000.00	7.200%	2,348,640.00	6,883,640.00
6/01/2007	4,865,000.00	7.200%	2,022,120.00	6,887,120.00
6/01/2008	5,215,000.00	7.200%	1,671,840.00	6,886,840.00
6/01/2009	5,590,000.00	7.200%	1,296,360.00	6,886,360.00
6/01/2010	5,990,000.00	7.200%	893,880.00	6,883,880.00
6/01/2011	6,425,000.00	7.200%	462,600.00	6,887,600.00
TOTAL	66,825,000.00	-	64,282,167.50	131,107,167.50

YIELD STATISTICS

Accrued Interest from 06/01/1991 to 06/01/1991...	-
Average Life.....	13.581 YEARS
Bond Years.....	\$907,540.00
Average Coupon.....	7.0831222%
Net Interest Cost (NIC).....	7.2112439%
Bond Yield for Arbitrage Purposes.....	7.0612483%
True Interest Cost (TIC).....	7.2724016%
Effective Interest Cost (EIC).....	7.2724016%

RESULTS

Schedules I, II and III illustrate the results of the analysis. Schedule I compares the cost of lease vs. build for the historical Justice Department Complex example. Schedule II provides this information for the hypothetical office analysis. Schedule III shows the annual debt service payments for the build options in both the historical and hypothetical examples.

a. Justice Department Complex

If the state had used lease revenue bonds to finance the Justice Department Complex rather than enter into a straight lease, it would save about \$30.7 million, on a present value basis, over a 50-year life of the building. The break-even point, or the amount of time it takes for the straight lease payments to equal the lease-purchase payments, is about 24 years. During the first five years of the lease, i.e. 1978 through 1982, the straight lease option is less costly by approximately \$7.4 million present value dollars.

b. Hypothetical Building Analysis - Straight Lease Rate \$1.15 Per Square Foot Per Month

For the hypothetical building, the 50-year present value savings is \$17.5 million with a straight lease rate of \$1.15 per square foot per month; the break-even point is at 34 years and the first five years straight lease benefit is \$16.4 million.

c. Hypothetical Building Analysis - Straight Lease Rate \$1.35 Per Square Foot Per Month

In the \$1.35 per month rent example, the 50-year present value savings is much greater, approximately \$39.1 million, reflecting the high degree of sensitivity lease rates have on the lease vs. build decision. For example, for the cost of leasing vs. a lease-purchase bond financing to be equal over a 50-year period, lease rates would have to be \$0.74. This is an exceptionally low office space rate and probably not available in the Sacramento area for the type of building and the location the state would rent.

The break-even point in the \$1.35 example is 25 years with the benefits of the straight lease after five years amounting to almost \$13.1 million.

RESIDUAL VALUE

Another important factor not included in the quantitative analysis is residual value of the asset. Residual value of an asset is its market value after a given point in time. In lease transactions, a schedule of residual value is determined by pricing the market value of the asset over its life. This is an important consideration for developers in determining their anticipated return on capital after specific periods of time. Estimating residual value is difficult in specific situations and is believed not to be practical in the foregoing analysis. However, including residual value in the analysis would favor the build option in the historical and "hypothetical" examples for the three time periods analyzed; 50 and five years and the break-even point.

Figure 1
Lease versus Purchase Costs
Hypothetical Model

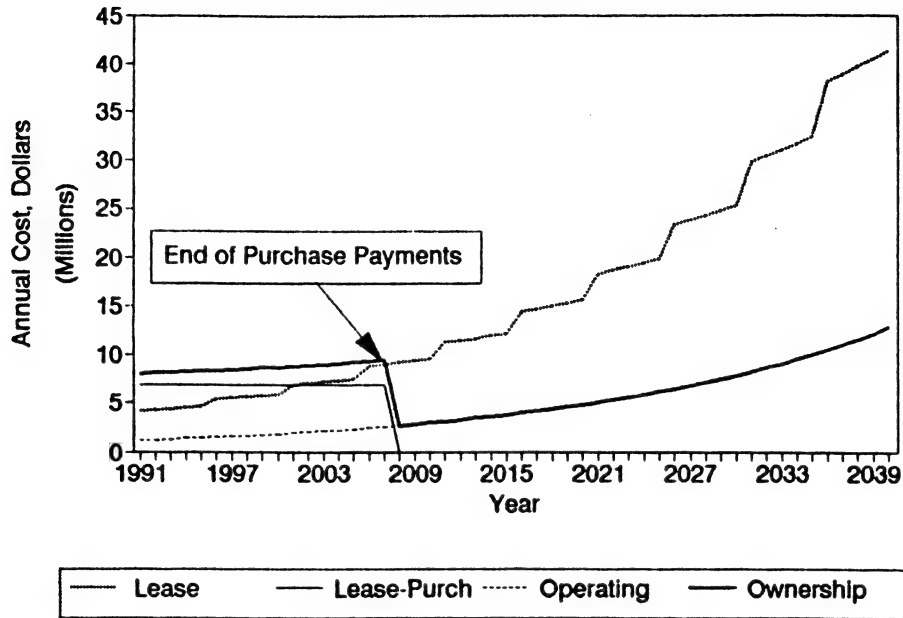


Figure 2
Cumulative Lease versus Purchase Costs
Hypothetical Model

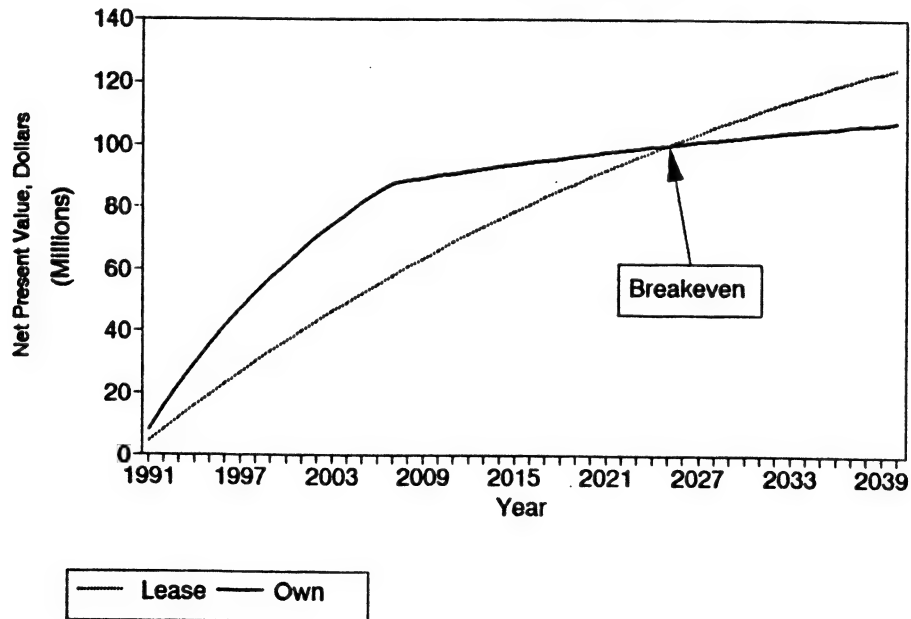


Figure 3
Cumulative Lease versus Purchase Costs
Historical Model

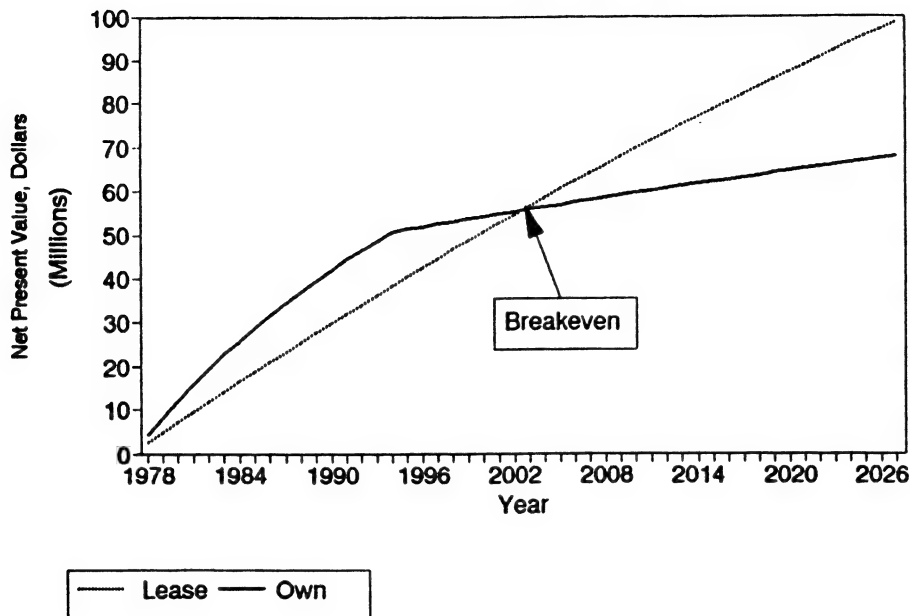
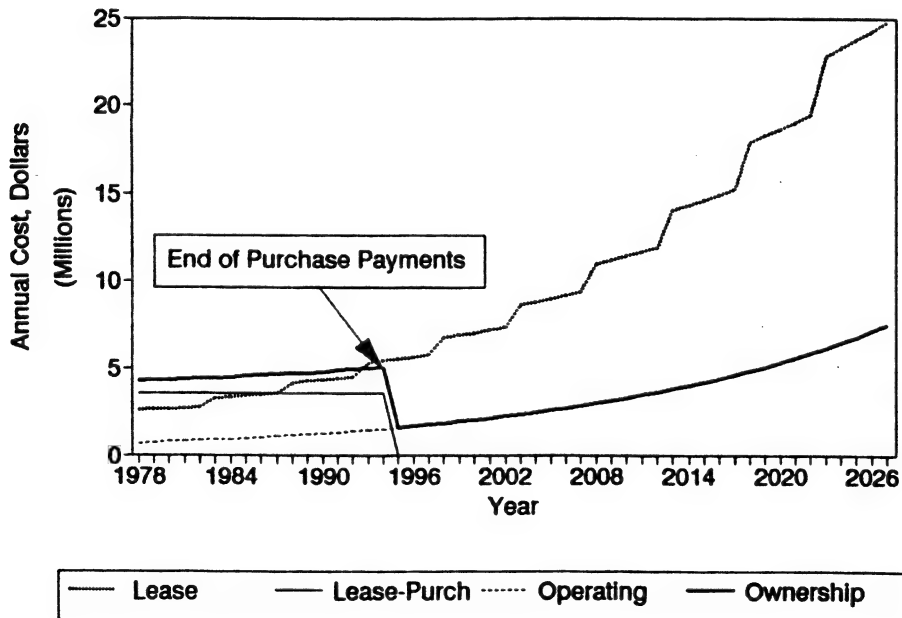


Figure 4
Lease versus Purchase Costs
Historical Model



In comparing the cost of the lease vs. build options, the residual value of the building and the amount of equity the state would have in the building should be included as added benefits in the lease-purchase alternative. This is especially important in the five-year and break-even time periods. Including residual value for these time periods would increase the benefits of ownership using lease revenue bonds.

CONCLUSIONS

Levels of Lease-Supported Debt

What level of lease revenue bond issuance can the state afford? To address this question, the general fund security for lease revenue bonds is briefly reviewed and then an integrated debt management process, that would assist policy makers to determine the level of lease revenue bonds the state may consider for funding office construction, is recommended.

In most state lease-supported debt structures, the underlying security for payment of debt service is the state's general fund. Lease payments are made from a department's annual general fund budget appropriation. The general fund, and a pledge of the state's full faith and credit, also secures the state's general obligation bonds. The level of lease-supported bond issuance, therefore, is dependent on the issuance level of general obligation bonds, given the assumption that the state's policy is to maintain its AAA/AAA rating (a lower rating will result in higher financing costs reducing the ability to support additional debt).

The guiding factors in determining the appropriate levels of general fund-supported debt (general obligation and lease supported) are the economic, financial, and administrative criteria rating agencies use to rate municipal debt. These factors should be used in developing an integrated debt-management model that assesses the impact of different proportions of additional general obligation and lease revenue bonds on the state's credit.

Clearly, the overwhelming effect on the state's credit is the pace at which it sells its authorized general obligation bonds. It is important to note that the state currently has approximately \$12 billion of unissued general obligation bonds. Lease revenue bonds for new building construction will have a much smaller effect on certain rating agency criteria, such as net-debt per capita, but will become increasingly important in the ratio that measures lease-supported debt to gross-bonded debt.

How can this information be used by DGS in its facilities planning process? The State Treasurer is responsible for managing the state's debt. It analyzes the impact of proposed state borrowing, for all purposes and types of bonds, on the state's credit. As part of an integrated office facility planning process, the State Treasurer's office can provide DGS with maximum annual lease revenue bonding levels for its Five Year Capital Plan (and beyond) given the anticipated rate of general obligation bond issuance. DGS, in turn, would develop a priority process to allocate among its projects the allowable level of annual lease revenue bond proceeds determined by the State Treasurer.

Not enough information about the State Treasurer debt management process is available to recommend how the information link between DGS and the Treasurer can be established. The institutional framework for this link should be considered, along with the other recommendations regarding the overall DGS office facility planning process.

"Is Building Cheaper Than Leasing?"

Considering a 50-year building life span, using lease revenue bonds to construct state office buildings is cheaper than leasing. Looking at a historical example and current conditions, the range of savings is in the magnitude of \$17.5 to 39.1 million dollars over 50 years. This is a savings of \$1.14 per square foot per year for the 307,305 NSF "hypothetical" building. Applying the \$1.14 savings to future construction in the Department of General Service's 1989 Five Year Capital Outlay Program, 2,599,723 NSF (converting the 3,209,535 gross square feet (GSF) in the plan to NSF using the same ratio of NSF/GSF as the Justice Complex, i.e., 81 percent), the annual saving is about \$3.0 million dollars per year. However, the outlook changes in the short-term view.

The smallest savings, attributed to straight leasing after five years, of the three examples is about \$7.4 million in the historical example, or \$4.84 per net square foot per year (\$7,400,000/5/307,305). Leasing the space scheduled for construction in the Five Year Capital Outlay Program would result in an \$12.6 million annual savings. But this savings does not consider the equity contributed by the state in the lease purchase option which is about \$6.6 million on a present value basis.

Clearly the answer to the query "Is it cheaper to lease or build" depends not only on the myriad variables contained in the analysis, but on one's time perspective. With a short-time horizon, it is cheaper to lease, not considering residual value. However, the state will have continuing needs for office facilities and should adopt the long-term perspective. The payoff in owning its buildings would start to accrue to the state after eighteen years or more, as shown in our historical example, but this does not take into consideration the equity the state accumulates in offices it builds with lease revenue bond financing. Based on conceptual review, it appears that it is cheaper for the state to build and own its facilities.

APPENDIX G FINANCING TECHNIQUES

INTRODUCTION

This appendix first describes financing techniques available to the state to fund its office space needs, and then recommends two financing methods related to tax-exempt borrowing the state could use to reduce its cost of financing office buildings. The recommended techniques are: 1) asset substitution to reduce capitalized interest costs and provide greater security to investors in lease revenue bond transactions, and 2) a short-term borrowing program to reduce the cost of construction financing.

DESCRIPTION OF FINANCING TECHNIQUES

The Department of General Services (DGS) and its consultants have produced several documents explaining the financing techniques available for funding state office buildings.² These techniques are organized into a flow chart and are briefly reviewed.

The chart has two basic financing categories, public and private. Private financing means that a taxable party, usually a developer (who pays federal, state and local taxes) is the owner of a building and provides his own equity and/or borrows in the taxable market to finance its construction. Once constructed, the developer negotiates with the state for use of the office space. The types of agreements the developer and the state may negotiate include leasing and lease-purchase arrangements.

Public financing implies public ownership and the use of tax-exempt borrowing and/or capital outlay funds to finance office construction.

Private Techniques: Leasing

a. Build to Suit

The state contracts with a developer to construct a building based on the state's required specifications. The developer owns and operates the building and leases it to the state.

b. Straight Leasing

This is the most common form of a lease entered into by the state. OREDS negotiates lease terms and conditions with the developer/owner of an existing building. The terms include the duration of the lease, base rent and operating and maintenance rental components, escalation rate for operating and maintenance costs,

²a. State of California, Financing Alternatives State and Consumer Services Agency, Department of General Services, task Force on Alternative Financing, November, 1983.

b. Sacramento Facilities Plan, Eighth Supplement, July, 1988.

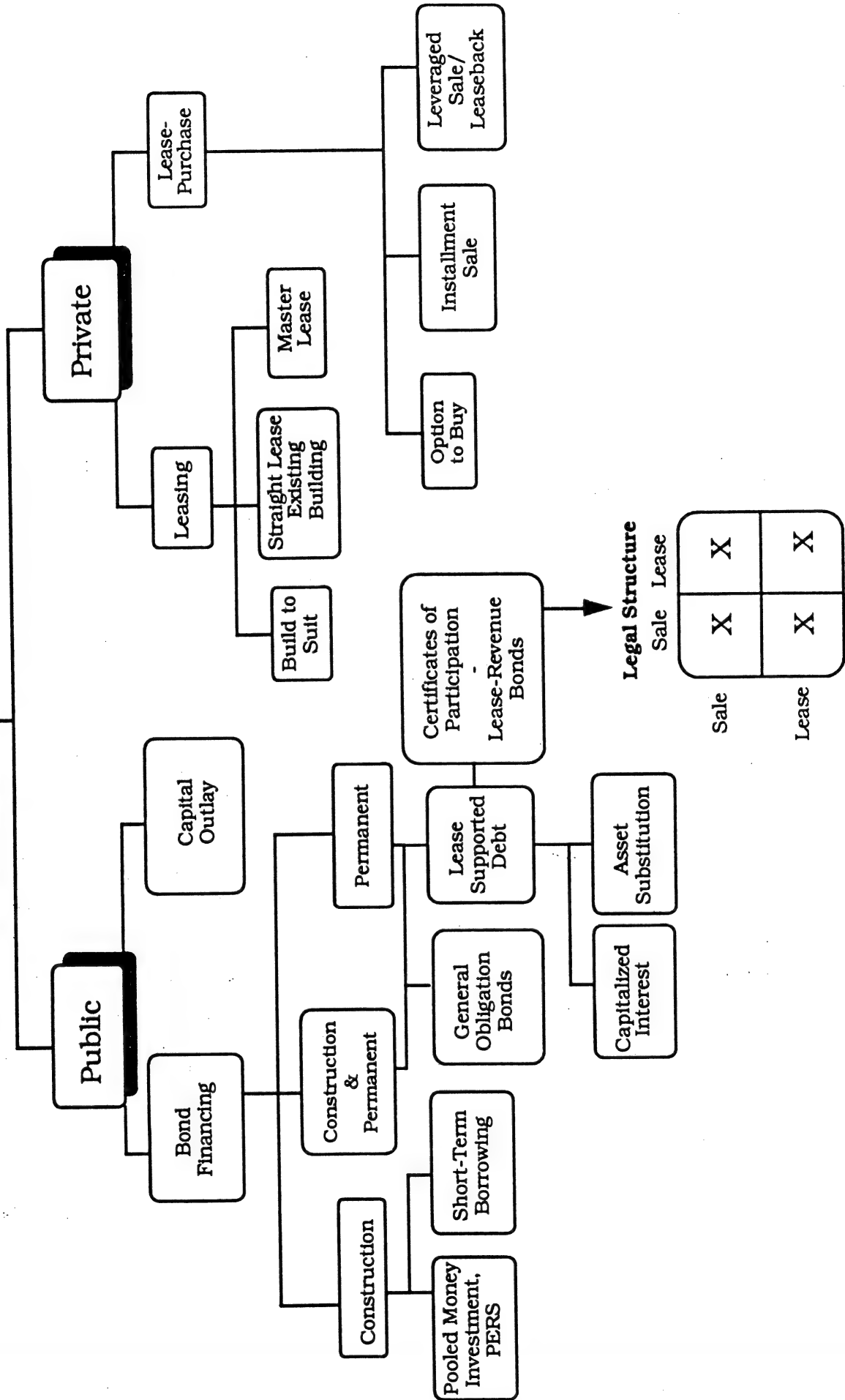
c. Deloitte, Haskins and Sells, State Property Management Demonstration Project, May, 1988.

d. Capitol Area Plan Progress Report, Office of Facilities Planning and Development, December, 1989.

e. Department of General services, Five-Year Capital Outlay Program, September, 1989.

Financing Techniques

Flow Chart



type of tenant improvements and other factors that determine the annual rent the state pays for the office space.

c. Master Lease

This technique was described in the 1988 Deloitte, Haskins and Sells State Property Management Project Report (p. D-12). It is basically the same as the straight lease, except the state would combine multiple leases with its largest landlords into one master agreement with standard terms and conditions. The intent of the master lease is to lower lease rates because of the volume of space occupied.

Private Techniques: Lease Purchase

a. Option to Buy

One of the terms and conditions of a straight lease may be an option to purchase the building after a specified period of time. At the option date, the state may purchase the building at the price indicated upon the signing of the lease agreement. OREDS has entered into several lease-purchase agreements and has exercised its option and bought buildings. However, the price of the building will reflect the developer's taxable cost of capital and rate of return, making it more expensive to buy than if the state had originally constructed the building with tax-exempt financing. Nevertheless, as long as the state continues to lease buildings from private parties, it should always include an option to purchase the building. The Economic Forecasting Model (EFM) can be used to help OREDS negotiate the option price and compare the cost of the lease-purchase with the straight lease over the economic life of the building.

b. Installment Sale

In this method the developer owns and constructs the building and negotiates annual installment payments with the state. At the end of the installment period title of the building is transferred to the state. This method is also more costly than state funding with tax-exempt bonds for office building construction because of the developer's taxable borrowing costs and required rate of return on his capital.

c. Leveraged Sale-Leaseback

This technique was used much more frequently before the 1986 Tax Reform Law changed depreciation and other tax benefits associated with real estate and limited the use of tax-exempt bonds in private transactions. The leveraged sale-leaseback involves the sale of a public facility to private investors and the leasing of the facility back to the public agency. The "leveraged" portion relates to the equity contribution made by a private owner over a five-year period, up to 20 percent of the purchase price, in exchange for the tax benefits received by the private owner. The tax benefits have to be equal to or greater than the return the private party expects to receive on its capital if they did not enter into the sale-leaseback transaction. Since the 1986 tax reform act eliminated most of the tax benefits associated with this type of transaction it is rarely used today. For more details about this financing technique, see "State of California Financing Alternatives," pp. 23-24.

Public Techniques: Capital Outlay

Capital outlay funds have traditionally funded the planning, design and construction of state office buildings. However, the availability of these funds for office construction has dramatically diminished because of Proposition 13, which reduced tideland oil sales, and restricted the use of capital outlay funds for the state's prison construction program and toxic waste cleanups (Capitol Area Plan Progress Report, December, 1989, p. 25.)

Reduced capital outlay funding means that the state rarely funds all of the stages of office building (preliminary planning, working drawings, land purchase and construction) with Capital Outlay funds. Because of the long capital outlay planning process, capital outlay funds are often available only for preliminary planning and perhaps working drawings. They have not been used for funding construction recently.

Because of its scarcity, Capital Outlay Funds need to be used as efficiently as possible. Consultants recommend that capital outlay be used to fund all planning activities up until the time the legislature approves construction of a building. At this point other financing techniques can take over to finance working drawings (if this phase occurs after approval) and construction.

Public Techniques: Bond Financing

The state can use bonds/notes to fund the construction period, as a permanent loan, or for both construction and permanent financing for its office buildings. It typically uses one bond issue for construction and permanent financing, as was the case with the Ronald Reagan Building in Los Angeles. However, financing options exist to split construction financing from permanent financing. In this case it has three ways to borrow money: from the Pooled Money Investment Board (PMIB), the Public Employees Retirement System (PERS), or with a short-term tax-exempt borrowing.

a. Pooled Money Investment/PERS

As discussed in the review of the Economic Forecasting Model, the state can borrow from PMIB for construction and repay the pool when it issues tax-exempt bonds. It can also borrow from PERS. However, these approaches are very costly, as the DGS would have to borrow at the PMIB or PERS earnings rates. The PMIB rate is a taxable money market rate that is 1.5 percent to 3.0 percent higher than a short-term tax-exempt rate. In addition, over 50 percent of the interest payments DGS makes on the PMIB loan benefits non-state municipal entities. If the state were to use this borrowing method, its General Fund (which pays debt service on the bonds issued to take out the PMIB loan) would subsidize other local governments' general funds. The PERS rate is even higher in that the retirement system's investments are much broader (stocks, bonds, real estate, money market instruments) and would usually have a higher earnings rate than the PMIB. In this case the state General Fund would subsidize state employees if DGS were to borrow from PERS. Another approach is to borrow in the short-term tax-exempt market.

b. Short Term Notes

Short-term notes in municipal finance are used for several purposes: to remove timing discrepancies between government expenditures and receipt of taxes and revenues (Tax and Revenue Anticipation Notes), as temporary financing until

long-term bonds are issued or grants received (Bond and Grant Anticipation Notes or "bridge financing").

Historically, the spread between short-term and long-term tax-exempt borrowing rates has varied from 200 to 300 basis points (2.0 percent to 3.0 percent). Even though the Treasury yield curve was inverted several times during the 1980s (i.e., short-term rates were higher than long-term rates), the municipal yield curve did not invert. The spread between long-term and short-term tax-exempt rates has only fallen under 200 basis points in 1980, late 1987 and recently (Standard and Poors, Credit Review, Municipal Short Term Debt, May 8, 1989, pp. 1-2).

To illustrate the potential savings of a short-term note borrowing, we will use the Hypothetical Office Building example discussed earlier. In this example, the state used lease revenue bonds to borrow \$66,825,000. The interest rate on the bonds ranged from 6.45 percent for the 1995 serial bond to 7.2 percent for the 2011 term bond based on the June 15 Delphis Hanover Index for AA bonds. The Bond Buyer Tax-Exempt Note rate for the same day (June 15, 1990) was 5.85 percent. Using the 7.2 percent rate for the fixed rate bonds, the difference between the short-term and long-term rates was approximately 135 basis points (1.35 percent). This is almost a one million dollar annual savings ($.0135 \times \$66,825,000 = \$902,138$) in interest expense, or about \$2.7 million over the three-year construction period.

In the context of financing office buildings, the state can use either fixed or variable rate short-term borrowing to reduce construction costs. A fixed rate short-term borrowing could be in the form of a Bond Anticipation Note (BAN). The state would issue a BAN whose maturity would extend to the end of the office building construction period. At that time, the state would refinance the note with a long-term lease revenue bond or certificate of participation. This approach is the same as the PMIB borrowing and repayment described in the review of the Economic Forecast Model except the cost of the construction loan (i.e. the Bond Anticipation Note), would probably be at least two percent to three percent lower than the PMIB borrowing rate. It would also be lower than the fixed rate for long-term bonds as discussed above. The drawback of short-term financing is the risk of an increase in long-term rates at the time of the bond refinancing that could nullify any savings realized by the note borrowing.

A variable rate approach to short-term financing is a commercial paper program. Commercial paper is a short-term tax-exempt borrowing instrument. It has a maturity of one to 270 days that can be structured to minimize interest expense. However, because of its short maturity the state would be exposed to a greater interest rate risk with commercial paper than with fixed rate short-term notes. This risk can be mitigated to some degree if the state is a frequent revenue bond borrower and expects to issue long-term bonds for construction projects on a regular basis. This is not the case with office buildings, as they are built infrequently. A viable commercial paper program would most likely be established state wide and only if debt management policy allowed for variable interest rate risk.

The state should use short-term note borrowing as a financial technique to reduce the cost of construction financing.

c. General Obligation and Lease-Supported Bonds

General obligation bonds and lease supported debt, either Certificates of Participation (COPS) or lease revenue bonds, are the borrowing techniques the state can use for construction and permanent financing. Although general obligation bonds are the least costly method of financing, to our knowledge they have not been used by the state to finance office buildings. To raise funds with general obligation bonds, the DGS would need an initial legislative ballot authorization, voter approval and legislative authorization for specific bond issues. Given the current level of voter-authorized but unissued volume of general obligation debt, approximately \$12 billion, it is highly unlikely that the legislature will allow general obligation issues for office buildings to be placed on the ballot. This leaves the lease-supported debt option.

Certificates of participation and lease revenue bonds are the two most common forms of lease-backed municipal securities. In a COPS financing, investors purchase a share (participate in) of an underlying lease revenue stream paid by a municipal lessee to either a public, private or not-for profit lessor. Lease revenue bonds are similar, in that the underlying security for debt service payments are the lease payments by the public lessee. The selection of a COP or lease revenue bond legal structure depends on the statutory, institutional, political, economic and financial circumstances of the assets being financed.

Several legal structural options exist in a COPS or lease revenue bond. The principal parties involved include a public lessor (or private and non-profit organization with COPS) as the issuing entity; a public agency lessee (who makes lease payments contingent on the beneficial use and occupancy of the facility); a trustee or fiscal agent; and investors. The assets involved in the transaction are real property (land and improvements) and/or equipment. The types of legal arrangements for COPS and lease-revenue transactions are shown on the flow chart, which includes a 2-by-2 matrix to indicate the potential level of complexity of lease transactions. These legal arrangements may take the form of a sale - saleback; sale-leaseback; lease-sale back and lease leaseback. The type of legal structure depends on the current ownership of land, improvements (if any) and the proposed changes to current ownership through the various sale or lease arrangements among the parties involved in the transaction.

The flow chart also shows two financing techniques associated with lease-supported debt transactions; capitalized interest and asset substitution. In the capitalized interest approach, the state issues a single long-term lease revenue bond or COP, whose proceeds include an amount sufficient to pay interest on the bonds during the construction period. Lease payments cannot begin until construction is completed because the lease requires that the lessee have the beneficial use and occupancy of the facility. By capitalizing interest the state obviates the need for separate construction financing. But capitalizing interest is a costly way of constructing office buildings. Since the construction financing is combined with permanent financing, the interest rate during the construction period is a long-term tax-exempt rate. By including the interest payments during the construction period the bond size is increased and debt service payments are greater if capitalized interest is excluded. For example, the present value savings of eliminating capitalized interest in our hypothetical building example is about \$12 million over the life of the bonds.

Asset substitution can reduce or eliminate the need to capitalize interest. Asset substitution is the replacement of a facility described in a lease that has not been

built with the lease of a facility that has already been constructed. An issuer would sell bonds supported by lease payments on a constructed facility and use the proceeds from the bond sale to build the proposed facility. With asset substitution the lessee can begin lease payments at the bond closing rather than after the facility is constructed because it has the beneficial use and occupancy of the facility. Asset substitution also is known as an "equity strip." The state's financing of the Avenal Prison is an example of an asset substitution.³

The State Public Works Board (PWB) issued \$104,000,000 of lease revenue bonds in 1985 to construct Avenal Prison. However, the lease supporting the transaction was not for the Avenal Prison, but the Southern Maximum Security Complex. The reason for the substitution was not to save capitalized interest expense, but because of a legal problem affecting the construction of the Avenal Prison. To affect the substitution the Southern Maximum Security Prison was effectively sold by the Department of Corrections for \$104,000,000 to PWB.⁴ The PWB sold lease revenue bonds to investors to pay for the purchase. The Department of Corrections leased the Complex back from the PWB and makes annual base rental payments equivalent to the debt service payments on the bonds. The proceeds from the bond sale were then used to construct the new Avenal Prison.

The substitution of the Maximum Security Complex in the lease for the unbuilt Avenal Prison saves the state money in two ways. First, the state does not pay capitalized interest, thereby reducing the bond size and annual debt service payments. Second, the state does not have construction completion risk for the leased facility. The Department of Corrections has the beneficial use and occupancy of the Southern Maximum Complex. Bondholders do not have to consider the risk of the facility not being completed on time so that lease payments can begin. They should be willing to receive a slightly lower yield for avoiding this risk, although it is very difficult to quantify this potential savings.

Asset substitution assumes that the appraised value of the building securing the lease is at least equivalent to the dollar amount of bond proceeds needed for constructing the new facility. In the example, the Department of Corrections had to find a substitute asset equal in value to the Avenal Prison. This requires knowledge of the state's unencumbered assets in general and prison assets in particular. If the state were to consider asset substitution for office and other lease-supported projects, then it should have a comprehensive list of unencumbered assets that can be used for substitution in lease financings. It is recommended that the state should add to the Proactive Asset Management data base a field(s) that includes the availability of the state assets for substitution in lease-revenue transactions. Depending on the state's policy regarding substitution, the data base should identify the unencumbered asset, its priority for substitution within the same department, and its availability for substitution with other departments.

The state should use asset substitution as a financing technique which reduces capitalized interest costs and provides greater security to investors in lease revenue bond transactions.

³The 1988 Sacramento Facilities Plan describes an asset substitution for building rehabilitation projects (p. 34, #5). This concept can be expanded to include new buildings.

⁴This is a general discussion of the legal structure. For a complete review of the legal structural aspects of the transaction, see the following bond documents: Bond Resolution; the Facility Lease Structural; and the Site Lease, \$104,000,000 State of Public Works Board of the State of California, Lease Revenue Bonds (Department of Corrections) 1985 Series A (Southern Maximum Security Complex).

APPENDIX H

POLICIES, OBJECTIVES AND ACTIONS FROM THE SACRAMENTO FACILITIES PLAN

This appendix presents the goals, policies and actions as set forth in the Sacramento Facilities Plan.

Goal: Between the years 1977 and 2000, state government shall provide office space in the state's capitol in a manner that will be consistent with the social, economic and environmental interests of the People of California.

Policy 1: State agencies and units thereof shall be consolidated in one of three planning areas according to functional and organizational criteria.

Action: Adopt the following as boundaries for the three planning areas of state facilities in Sacramento.

- (1) core area/Capital Area Plan (CAP) -- that area within a ten-minute walk of the state Capitol, including contiguous properties.
- (2) Central city -- Bounded by American and Sacramento Rivers, north and west respectively and by W-X and 29th-30th Street freeway corridors, south and east respectively, plus selected contiguous areas. Excludes Core area.
- (3) Metropolitan Sacramento -- All of metropolitan Sacramento excluding the core and central city area described above.

Action: Locate agencies and units thereof in the Core area if most of the following criteria are met:

- (1) Has statewide functions and responsibilities;
- (2) Has expressed a desire to be in the Core area;
- (3) Has functional and organizational relationships with other governmental entities that require frequent face-to-face or mail communication;
- (4) Has an organizational relationship to other entities (agency's secretaries, constitutional officers, legislature, Governor, etc.);
- (5) Meets the above criteria and has a small local or regional staff which can be served more efficiently by its parent unit's office staff;
- (6) Has not already developed and/or occupied office facilities specifically designed for that agency's particular unit (e.g., DMV, Justice);

(7) Does not have special space intensive requirements (warehouses, corporation yards, laboratories).

Action: Locate agencies and units thereof in metropolitan Sacramento or in areas contiguous to the central city if most of following criteria are met:

(1) Agency has a statewide function but has space intensive needs in conjunction with office space (e.g., corporation yards, laboratories, security, warehouses);

(2) Has a function relating to administration and operation of regional offices overseeing or regulating activities of field units; and/or

(3) Serves or conducts business with clientele in a specific geographic location.

Action: Develop and accelerate a state office building program to accommodate existing and projected demand in Sacramento.

Action: Adopt the proposed Capitol Area Plan building program.

Action: Develop separate building and rehabilitation programs for the central city and metropolitan Sacramento planning areas to complement the Capitol Area Plan building construction program.

Policy 2: Allocation of office space on a priority basis shall be based upon agency needs and cost savings.

Action: Allocate office space on a priority basis to those agencies meeting all, or portions, of the following criteria:

(1) Agency occupies space with 0-5 year lease terms.

(2) Rents for leased space are higher than other comparable space in the Sacramento area.

(3) Agency expects employee expansion within the next 5-10 years that would require the leasing of office space in the absence of vacant state-owned spaces.

(4) Agency currently occupies poor quality space.

Action: Based upon the Capitol Area Plan's building construction program, allocate space to the agencies noted in the following illustrations (Buildings Sites 1 through 7).

NOTE: The following are the basic steps involved with allocating and backfilling space. Each step is numbered to correspond with illustrations for building sites 1 through 7. A legend

and consolidation code is also included to explain the symbols used in the illustrations.

Policy 3: Set into action a prompt and serious commitment to the efficient use of energy including immediate development of renewable energy resources in the Sacramento area.

Action: Perform energy-oriented audits on state buildings, establishing technical baselines and energy conservation programs for individual buildings.

Action: Change systems of building operations and maintenance methods to incorporate energy conservation practices.

Action: Request funding for retrofit conservation projects, using life cycle benefit/cost analysis for the alternatives to achieve the greatest energy savings for dollars invested.

Action: Install solar heating and water heating devices wherever practical.

Action: Institute an employee awareness campaign of energy conservation methods and needs.

Action: Incorporate energy conservation incentives for lease option properties.

Action: Develop energy performance as a major consideration in the planning and design of all new state buildings in metropolitan Sacramento area.

Action: Establish minimum design criteria responsive to Sacramento's climate characteristics.

Action: Improve planning considerations in locating facilities to minimize transportation energy used by commuting employees, visitors, and inter-office travel.

Action: Develop transportation patterns as a major consideration in the planning of new state buildings and leasing of private facilities.

Action: Encourage alternatives to single occupant vehicles, such as ride-sharing, bicycling, walking, mass transit.

Action: Improve the energy efficiency of state-owned fleet and mobile equipment through procurement practices and operational methods.

Action: Participate with local entities in promoting alternatives to single occupant vehicles through development of park and ride facilities, bike lanes, etc., for state facilities.

- Action:** Locate state operations to encourage use of ride-sharing, bicycling, walking and mass transit.
 - Action:** Develop the state's role in improving the overall-integrated energy patterns of the Sacramento area.
 - Action:** Encourage cooperative efforts by state and local entities in energy programs, including federal money for projects (e.g., waste heat utilization) in the Sacramento area.
 - Action:** Identify and correct institutional barriers to efficient use of energy resources.
 - Action:** Participate in waste recycling programs and community gardens in the Sacramento area.
 - Action:** Rehabilitate existing state facilities and design new buildings to reduce peak load requirements on the Sacramento Municipal Utility District network and the state's Central Heating and Cooling Plant.
 - Action:** Improve the state's participation in the development of alternative transportation corridors (e.g., bus stop protection).
- Policy 4:** Consolidated and dispersed facilities shall be in areas where the general public and the state's employees have easy access to public transport facilities.
- Action:** Coordinate site selection of proposed or existing owned or leased facilities with the Sacramento Regional Transit District to assure transit facilities serve or will be provided before a site is acquired or leased.
- Policy 5:** Existing and future space requirements will be satisfied by leasing and acquiring new structures and/or rehabilitating existing office structures.
- Action:** Acquire approximately 90 percent and lease 10 percent of all office space required.
 - Action:** Based upon total existing and projected demand, allocate leased and acquired office space to agencies by planning area.
- Policy 6:** Acquired or leased space shall be developed in areas where the presence of state's facilities and activities can enhance the social, economic, and environmental quality of a community.
- Action:** Include in site selection activities an analysis and evaluation of alternative sites that will address the social and economic impacts of the state's activities and functions in the neighborhood communities most directly affected.

Policy 7: Financing of new construction and rehabilitation of office facilities shall be based upon the most economical means available.

Action: In addition to the capital outlay appropriations, other financing options, including general obligation bonds, joint powers authority, non-profit corporations, lease-purchase from private corporations, lease-purchase from private developer and lease with purchase options from a private developer, shall be evaluated as to the most economic method of financing.

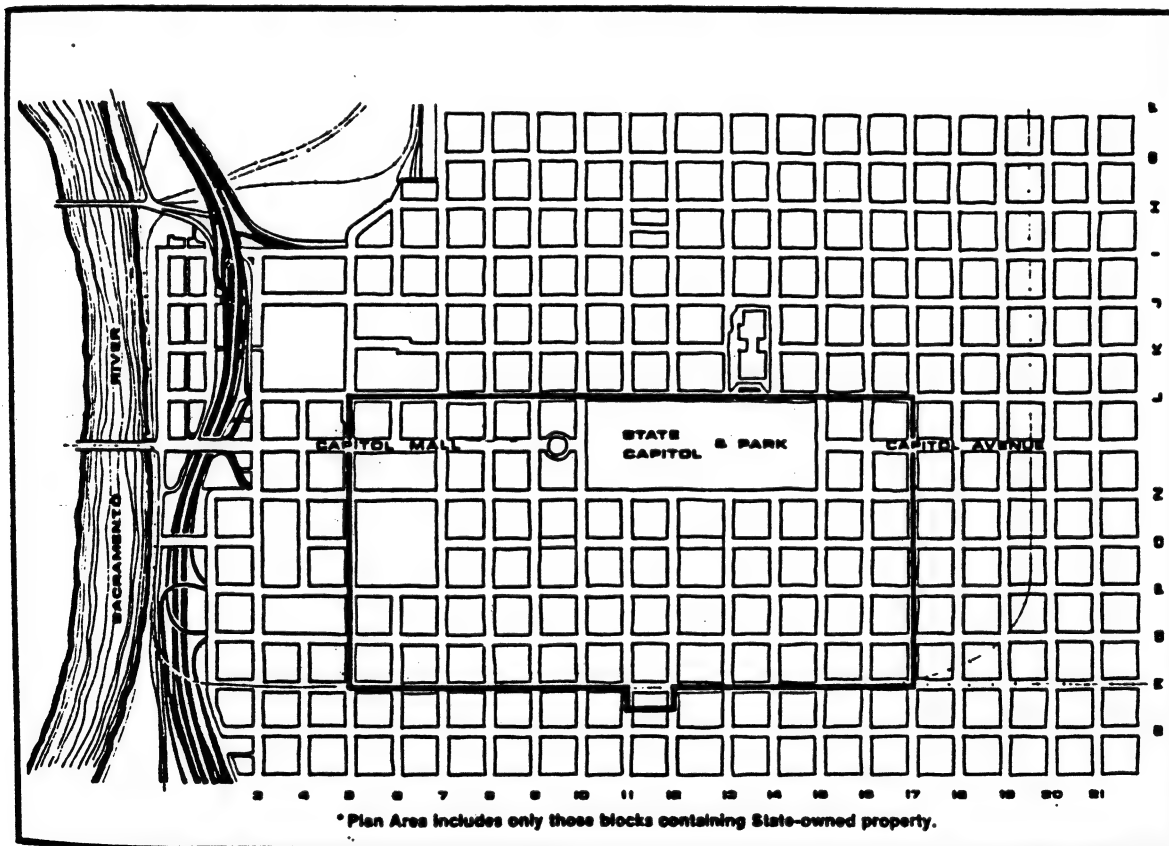
APPENDIX I DEFINITION OF THE PLANING AREAS IN THE CAPITOL AREA PLAN⁵

Core Area: That area within a ten-minute walk of the State Capitol, including contiguous properties. This is the area bounded by 'G' Street on the North, 'R' Street on the South, 5th Street on the West and 17th Street on the East⁶.

Central City: The area bounded by the American and Sacramento Rivers, North and West respectively and by 'W' to 'X' and 29th to 30th Street freeway corridors, South and East respectively, plus selected contiguous areas. Excludes the Core Area.

Metropolitan Sacramento: all of Metropolitan Sacramento excluding the Core and Central City areas as described above.

Plan Boundaries: The boundaries of the area governed by the Capitol Area Plan are shown on the following map, which is taken from the Capital Area Plan document.



⁵The definitions are taken from the Sacramento facilities Plan, 1977-2000, Department of General Services (DGS), Long Range Facilities Planning Office, Sacramento, April 1977; P. 37

⁶Specific boundaries of the Core Area taken from the Sacramento Facilities Plan, 8th Supplement: Implementation Issues, DGS, Office of Project Development and Management (OPDM), Sacramento, July 1988, P. 2 & 5

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Memorandum

To: Kurt R. Sjoberg
Acting Auditor General
660 J Street, Suite 300
Sacramento, CA 95814

Date: August 10, 1990


From: Office of the Secretary
(916) 323-9493
ATSS 473-9493

Subject: RESPONSE TO AUDITOR GENERAL REPORT NO. C-972

Thank you for the opportunity to respond to your Report C-972 entitled "A Study of the State's Office Space Facilities Planning Goals, Policies and Recommendations". The attached response from the Department of General Services addresses each of your recommendations.

If you need further information or assistance on this issue, you may wish to have your staff contact W. J. Anthony, Director, Department of General Services, at 445-3441.

Sincerely,


SHIRLEY R. CHILTON
Secretary of the Agency

SRC:mb

cc: W. J. Anthony, Director,
Department of General Services

Rick Gillam, Audit Coordinator
Department of General Services

MEMORANDUM**Date:** August 10, 1990**File No:** C-972**To:** Shirley R. Chilton, Secretary
State and Consumer Services Agency
915 Capitol Mall, Suite 200
Sacramento, CA 95814**From:** Department of General Services**Subject:** RESPONSE TO AUDITOR GENERAL REPORT NO. C-972 -- A STUDY OF THE STATE'S OFFICE SPACE
FACILITIES PLANNING GOALS, POLICIES, AND RECOMMENDATIONS

Thank you for the opportunity to respond to Office of the Auditor General (OAG) Report No. C-972. This report was prepared under contract for the OAG by the Institute for Law and Policy Planning (Consultants). At the request of the OAG, the Department of General Services (DGS) will only respond to issues directly related to its operations. This request was made because the primary recommendations in the report relate to State, defined as the administration and the legislature, policy issues and not to DGS responsibilities.

In Chapter 8, the report addresses recommendations to DGS. The following response addresses each of those recommendations. For the issues and recommendations which do not directly apply to DGS, we have provided our comments for informational purposes. This information is provided after the words "DGS Comments". Recommendations related to DGS operations are responded to after the words "DGS Response". Because of the length of the report, and the extensive level of detail provided, the DGS will not attempt to respond to all of the issues reported. However, DGS staff will study the feasibility of addressing all of the issues. In addition, DGS staff will be available to further discuss these matters with interested parties.

OVERVIEW OF REPORT

The DGS has reviewed the report prepared by the Consultants and has concluded that it provides an excellent discussion paper for future planning activities related to the Capitol Area and the Sacramento Facilities Plans. The Consultant's study within DGS primarily involved analysis, evaluation, and recommendations on the procedures and available resources of the Office of Project Development and Management (OPDM), and the policies under which it operates. Therefore, we are pleased that the Consultants find in the report's Executive Summary "that OPDM's procedures are well-suited to perform the task with which they have been charged."

The DGS appreciates the objectivity shown by the Consultants in preparing, within a short timeframe, a thorough study of the Capitol Area and Sacramento Facilities Plans. While further efforts are necessary to determine the reasonableness of a number of recommended actions, overall, the report's recommendations will be helpful in improving the State's planning process.

REPORT CHAPTER 8 RECOMMENDATIONS LEADERSHIP

RECOMMENDATION: "The State of California, including the new administration and the legislature, must decide if it still wishes to implement the Capitol Area Plan and the Sacramento Facilities Plan. If it does (or has only minor modifications), a clear commitment to do so is required."

DGS COMMENTS: By December 31, 1990, the DGS will prepare a transition paper for the new administration to advise it of the history of the problem, key issues, alternative courses of action and the implications of those choices.

PLANNING STRUCTURE

RECOMMENDATION: "The state should examine and revise the existing planning structure to enable better implementation of the policies." This recommendation provides for the establishment of a high-level policy making body, the reorganization of the planning function to a single office, and the defining of the responsibilities of this new office.

DGS COMMENTS: The DGS notes that it is important that the planning structure be considered in the context of the entire capital facilities program. Changes which improve programs examined in the Consultant's study may worsen conditions for other programs; therefore, a thorough analysis is warranted before embracing these recommendations.

REVIEW OF PLAN ASSUMPTIONS

RECOMMENDATION: "The Sacramento Facilities Plan and the Capitol Area Plan should be reviewed and the goals modified when warranted by changing conditions or flawed assumptions. With the exception of these modifications, the original goals of the plans should be maintained and supported. Specific areas that should be reviewed are listed below.

- . Development north of L Street should no longer be a goal.
- . It is not necessary to adhere rigidly to the quarter-block development concept, particularly for parking structures. The spirit of the plan can be maintained by promoting mixed-use development on adjacent blocks.
- . The goal of reducing the proportion of single-occupant vehicles to five percent by 2000 is unattainable; this figure should be raised to a realistic level.
- . The reduction of leased space remains highly desirable, but leasing should be used for short-term needs and whenever else it is truly advantageous. The fraction of leased space will change with conditions and should not be forced into an arbitrary fixed value of ten percent, which is probably unrealistic."

DGS RESPONSE: While items such as these are periodically discussed before the Capitol Area Plan Committee, the DGS will specifically put these matters on the agenda of the next meeting of this Committee. At that meeting, which is planned for September or October, OPDM staff will present background information and request comments and direction regarding the changes. Unless Committee members recommend against, we would anticipate that the adopted changes will be reported in the 1990 Progress Report on the Capitol Area Plan.

FINANCING METHODS

RECOMMENDATION: "The state should seek long- rather than short-term economic benefits in space acquisition. Even though capital outlay would be the cheapest way to build, the funds are not available. Alternative financing, generally by lease-revenue bonds, should be the first choice in most development proposals.

- . The state should continue to actively review and evaluate alternative financing routes.
- . The state should explore the feasibility of purchasing existing buildings, especially those it presently occupies."

DGS COMMENTS: For a number of years, the State has used lease-revenue bonds to fund capital outlay projects. This fact is restated in DGS' September 1989 Capital Facilities Plan which established lease-revenue bonds as the first choice for funding most major facilities.

In an ongoing effort to identify and understand the tools available for financing projects, alternative financing methods for both general and specific application will continue to be examined in consultation with the State Treasurer's Office, State and local agency representatives, consultants, and the private sector real estate community.

Purchase of existing buildings is a course the State has considered in the San Francisco Bay Area in the effort to consolidate the Department of Transportation's District 4 office operations. It has been found that issues related to competitive bidding and building codes (local rather than Title 24) can be troublesome but are not unresolvable. Further, a potential difficulty in Sacramento with acquiring currently occupied facilities is that many are in designated redevelopment areas. Redevelopment agencies rely upon tax increments from privately-owned commercial office and retail property to pay taxes to fund housing and other redevelopment activity. Therefore, public benefit may be perceived differently by local and State decision makers.

Straight Leasing vs Lease Purchase (Bond Financing)

RECOMMENDATIONS: The following recommendations are provided in this area:

"The state should own the buildings required for office space rather than use a straight lease to accommodate this need. Ownership applies to existing and future buildings. Tax-exempt bonds and/or notes should be used to buy existing buildings or raise money for new buildings.

- . Whenever the state negotiates a straight lease, it should always negotiate an option to purchase the building.
- . In most circumstances, the state should not use private installment sale financing to take ownership of a building at the end of the rental payment period unless it is not able to finance ownership with tax-exempt bonds."

DGS COMMENTS: Upon appropriate economic evaluation, State ownership rather than leasing of a building may be advantageous, and tax-exempt bonds and/or notes may offer rates more favorable than conventional financing. However, we caution that there are circumstances under which leasing is preferable, and the DGS has advised client agencies accordingly. For example, because of the length of the Capital Outlay Budget Process, agencies are better off in leased space than they are in a State-owned facility if they have a need for frequent expansion or alteration, have a specific locational requirement, or have a demand too small to support development of a State-owned building.

We question whether a purchase option should always be negotiated when the State executes a lease. There are circumstances under which the State must accept the only space available, rather than space actually suitable for a particular agency. We prefer that the recommendation be preceded by, "In most circumstances," rather than, "Whenever". It also should be noted that as provided in Government Code Section 14669 the Director of DGS is prevented from entering into a lease-purchase agreement, or a lease with an option to purchase with an initial option purchase price over two million dollars, either of which involves office space, unless specifically authorized to do so by the Legislature.

Because of changes in tax law, it is currently not feasible to use the private installment sale financing method to acquire a building. If this financing method becomes feasible at a later date, while not preferred, this will be another method considered when analyzing funding alternatives.

The Master Space Planning Process

RECOMMENDATIONS: The following recommendations are provided in this area:

- . "The State Treasurer's office should provide DGS with an annual amount of bonding (lease revenue bonds and/or certificates of participation) that it believes the State's general fund can support for the Department's Five Year Capital Planning Process.
- . The Master Space Planning Process would establish policies and criteria to allocate the available annual bond volume between new office construction for DGS' Five Year Capital Plan and the purchase of existing buildings."

DGS COMMENTS: It should be noted that this finding implies that only the DGS has a Five Year Capital Plan. In actuality, all State agencies have their own plan. While the DGS has a long-standing, cooperative relationship with the State Treasurer's Office, if these recommendations are implemented, we believe it would be more appropriate that the annual amount be communicated to the Department of Finance, where all Capital Plans can be evaluated, and the respective shares for competing agencies can be allocated.

Financing Techniques and the Economic Forecasting Model

RECOMMENDATIONS: The following recommendations are provided in this area:

- . "The state should include asset substitution and short-term note financing alternatives in the Economic Forecasting Model (EFM).
- . When selecting an "average coupon yield," the state should determine whether the rate used already incorporates the underwriter discount fee and other costs of issuance.
- . If the proceeds of a bond issue (except the debt service reserve fund) can be spent in two years according to the following schedule:
 - 10 percent spent within 6 months
 - 45 percent spent within 12 months
 - 75 percent spent within 18 months
 - 100 percent spent within 24 months

the state should use the earning's rate from the Pooled Money Investment Board as the earning's rate in the EFM bond's construction and capitalized interest fund. If the construction period is greater than two years, then the state should use the arbitrage yield of the bonds as the earnings rate for the construction, capitalized interest and debt service reserve funds.

- . For each asset in the Proactive Asset Management data base, the state should indicate whether it is available to use as collateral in a lease revenue bond financing.
- . When planning a bond issue for office construction, the state should identify assets in the Proactive Asset Management data base that can be leased as a substitute for the lease on the proposed new building. The state should use the asset as a substitute whenever possible to eliminate capitalized interest expenses.
- . When planning a bond issue, the state should evaluate the use of short-term tax-exempt financing during the construction period.
- . The effect on the tax-exempt status of bonds issued for a state-owned building that has space for "non-public" purposes such as cafeterias, concessions, and child care needs to be further explored."

DGS RESPONSE: OPDM will update the EFM during the 1990-91 fiscal year. The feasibility of incorporating the recommended additions will be explored, and if possible, the EFM will be modified. With respect to use of the Proactive Asset Management data base, OPDM and the Office of the Real Estate and Design Services (OREDS) will explore the implications and the feasibility of implementing the recommendations. Consultation will also continue with parties outside DGS (State Treasurer's Office, underwriters, bond counsel) to formulate a position on the use of short-term issues during construction, and "non public" uses and their implications for tax-exempt issues.

It is anticipated that information with respect to these matters will be reported in the 1990 Progress Report on the Capitol Area Plan.

THE CAPITAL OUTLAY FUNDING PROCESS

RECOMMENDATION: "Unless capital outlay funds once again become plentiful, they should be used only for the preconstruction stages of a project and for major repairs. Construction of a building should not be dependent on the availability of capital outlay funds.

- The funding process should be streamlined, when possible, to reduce substantially the time required to construct new facilities.
- After a building project is initially approved, it should not be subject to cancellation or long delays, except in the most extreme and unusual circumstances.
- The state should consider establishing an independent authority (or empowering CADA) to develop projects free from annual political review once those projects are approved by the governor and the legislature."

DGS COMMENTS: Currently, the DGS has two major facilities (State Archives and Franchise Tax Board - Phase II) under development which used funding from capital outlay for preliminary planning and other funding alternatives from that point forward. DGS' Five Year Capital Plan already recommends that once projects are initiated, if capital outlay funds are not available, the project should go forward by alternate means. The DGS is also currently testing the use of CADA as a vehicle for developing a small building. The advantages and disadvantages of this alternative will be assessed throughout the process. Upon completion, the DGS will report its findings in the appropriate annual Capitol Area Plan Progress Report.

PLANNING POLICIES AND PROCESS

Since most of the following recommendations apply to DGS responsibilities, a separate response or comment is provided for each recommendation.

RECOMMENDATION: "Updating and maintenance of the CAP and the Sacramento Facilities Plan should include more detailed annual agency surveys. Employee transportation patterns should be sampled every two years."

DGS RESPONSE: The current in-progress agency survey requests additional details from agency managers with respect to telecommuting, satellite office complexes, and program locational needs. The results will be reported in the Ninth Supplement to the Sacramento Facilities Plan which should be completed by February 1991.

For the last ten years, employee transportation patterns have been sampled every two years by OPDM. OPDM is also currently processing a contract with Chico State University which includes provisions for the sampling of travel patterns on a regular basis.

RECOMMENDATION: "The location and consolidation study addressed in the Sacramento Facilities Plan should be updated. It should provide a systematic and rational guide to locating agencies in the core area. This analysis should be made part of the State's ongoing planning activities."

DGS RESPONSE: An update of the location and consolidation study will be included in the Ninth Supplement. In addition, the DGS will explore the feasibility of extracting a portion of the information from the Proactive Asset Management data base.

RECOMMENDATION: "The consolidation and locational criteria should include multidepartmental consolidation and should recognize proximity to the capitol as a scarce resource."

DGS RESPONSE: DGS expects that the agency survey now being conducted will provide a sound basis for developing criteria for multidepartmental consolidation. In addition, it is expected that the developed criteria will assist the DGS in allocating space near the Capitol.

RECOMMENDATION: "A detailed systematic assessment of the condition and rehabilitation status of all older buildings in Sacramento should be made."

DGS COMMENTS: Although we do not deny that the assessment would be helpful in an overall analysis of what course of action may be appropriate, the DGS cautions that there would be a substantial cost in assessing the buildings, and that the results would still not address the related planning, environmental impact, or overall real estate portfolio issues.

RECOMMENDATION: "The Statewide Property Inventory should be the data base supporting the planning. The planning office may find it necessary to augment data from the SPI with information of its own, but it should not set up a separate and perhaps inconsistent data base."

DGS RESPONSE: OPDM has worked with OREDS to ensure that specific fields were incorporated into the design of the SPI. In addition, it is anticipated that by July 1991 OPDM's data on employees will be fully merged with SPI. It is not yet clear whether it is feasible to use the SPI to calculate and report forecasts of space needs, or if a separate system is more cost effective, but it is anticipated that OPDM and OREDS will share the same data base.

RECOMMENDATION: "A leasing policy consistent with the consolidation and location goals of the CAP should be developed and instituted."

DGS COMMENTS: Consolidation has long been a goal of leasing activities undertaken by DGS. In the last three years, the DGS has accomplished consolidation of major operations of the Board of Control and the following departments: Transportation, Corrections, Personnel Administration, and Housing and Community Development. Other activity is in progress to consolidate the Department of Consumer Affairs, the Air Resources Board, the Integrated Waste Management Board, the State Treasurer's Office, and the Board of Equalization. All these actions are consistent with the Capitol Area Plan.

RECOMMENDATION: "The state should evaluate the success of the specially-designed and experimental buildings constructed in the early 1980s and incorporate the results into the plans for future facilities."

DGS COMMENTS: The DGS anticipates that the recommended study would be conducted if similar alternative methods are proposed in the future; however, these methods are not currently being proposed. Buildings now in design and development are not experimental in nature.

RECOMMENDATION: "Other factors in addition to department heads' predictions should be used to forecast staffing and space needs. Overall Sacramento area staffing as well as individual agency requirements should be examined."

DGS RESPONSE: As noted in Appendix D of the report, "OPDM is employing reasonable procedures for staffing projections." DGS acknowledges that there is value in considering as many factors as possible when developing projections. While agency data will continue to be the primary source of projections, as determined to be feasible, OPDM will validate this data.

RECOMMENDATION: "The sizes of core area and peripheral parking facilities should be reexamined in light of the revised transportation mode split goals."

DGS RESPONSE: OPDM expects the results of its 1990 Travel Survey to be available by mid-October. After receipt of the survey, the DGS expects to discuss the matter of revision of the mode split goals with the Capitol Area Plan Committee. Any action taken will be reported in the 1990 Progress Report on the Capitol Area Plan.

RECOMMENDATION: "If peripheral parking is to be retained, incentives such as subsidizing the parking fees and shortening the shuttle bus transit times will need to be developed."

DGS COMMENTS: The DGS will continue to evaluate the peripheral parking lot issue, but it has been our experience that demand for the spaces has risen as parking rates near the Capitol area have gone up, residential parking permit programs have been adopted, on-street parking meters have been added and rates raised, and as surface lots have been developed. Peripheral parking has been an integral part of the Plan since its adoption.

RECOMMENDATION: "Provision for telecommuting and child care should be explicitly included in the revised plans."

DGS RESPONSE: The Ninth Supplement of the Sacramento Facilities Plan will incorporate telecommuting. In addition, child care issues will be addressed once the DGS has adopted its Child Care Master Plan which is scheduled for completion no later than July 1, 1991.

RECOMMENDATION: "The planning office should prepare an introductory guide to the planning and financing process for use by department administrators, legislative staff, and other involved parties. It should also maintain a concise history of the progress of projects under its jurisdiction."

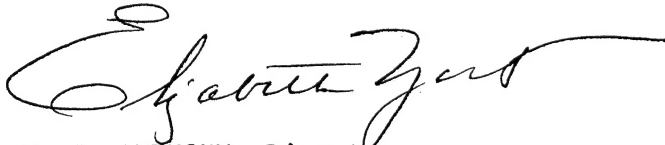
DGS COMMENTS: The DGS assumes that the planning office referred to under this recommendation is the new office recommended for establishment under the Planning Structure Section of Chapter No. 8. Currently, the DGS has basic information packages available for those interested in planning and financing; however, for planning activities, experience has shown that detailed information packages must be tailored to the individual client.

Active projects within DGS are tracked through the Five Year Capital Plans. Those Plans are submitted annually to the Department of Finance.

CONCLUSION

As part of its continuing efforts to improve policies and procedures, the DGS will take appropriate actions to address the issues presented in this report. We appreciate the constructive manner in which the study was conducted.

If you need further information or assistance on this issue, please call me.

A handwritten signature in black ink, appearing to read "W. J. Anthony", with a stylized flourish extending from the end.

W. J. ANTHONY, Director
Department of General Services

WJA:PH:RG:kg

**cc: Members of the Legislature
Office of the Governor
Office of the Lieutenant Governor
State Controller
Legislative Analyst
Assembly Office of Research
Senate Office of Research
Assembly Majority/Minority Consultants
Senate Majority/Minority Consultants
Capitol Press Corps**